OFFICIAL OPINION NO. 88-32, Venture Capital

August 3, 1988

Mr. Dan L. Kirby, Chairman
South Dakota Investment Council
Security Building, Mezzanine 120
101 South Main
Sioux Falls, South Dakota 57102-0571

Official Opinion No. 88-32

**RE: Venture Capital**

Dear Mr. Kirby:

You have asked for my opinion concerning the following factual situation:

FACTS:

Several issues have been raised relating to the investment by the Investment Council of South Dakota of cash flow funds in venture capital funds as contemplated by H.B. 1233 (1986). [SDCL 4-5-26(6)] There have been substantial previous discussions (and research) on various aspects of these issues between your office and the Governor's Office of Economic Development. After consultation with all of those involved, I now believe we have formulated these inquiries in a way which will answer the Council's questions about its venture capital options under South Dakota law. Except as otherwise stated, all questions are limited to the cash flow funds rather than the investment of South Dakota Retirement System or other monies managed by the Council.

It has been suggested from time to time that investment in venture capital is by its nature so risky as to fall outside the prudent-man standard. Others have suggested that any such presumption is overcome only by the specific enumeration of this investment vehicle in Section 4-5-26(6). Still others believe prudent investors can and do invest limited portions of a portfolio in venture capital investments without specific statutory authority.

The term "venture capital" is defined in Webster's New Collegiate Dictionary (1979) as: "capital (as retained corporate earnings or individual savings) invested or available for investment in the ownership element of new or fresh enterprise--called also risk capital". To the Council, that sounds like a definition of equity.

We are advised that the absence of specific authority in the Constitution [S.D. Const. Art. XIII, § 1] to invest in equities and the 1936 deletion of the language to that effect raises a negative presumption here. We are requesting your opinion whether the specific authorization provided by SDCL 4-5-26(6) overcomes that presumption.

The fact seems to be that if the Constitution prohibits the investment of South Dakota cash flow funds in equities, no meaningful venture capital investments can be undertaken by the Investment Council through the cash flow funds.

We very much appreciate your clarification of these issues for us. A substantial majority of the members of the Council continue to be interested in investing cash flow funds in qualified venture capital funds under the law and our regulations. At the same time, we are unanimous in our resolution to comply with the law and to explore other legally acceptable options if those discussed in this letter are foreclosed.

Based upon these facts, you have asked the following questions:

QUESTIONS:

1. Is the legislative delegation to the Investment Council of power to invest in venture capital funds an unlawful delegation of authority?

2. May the prudent-man standard of Section 4-5-27 be met by investment in venture capital funds pursuant to Section 4-5-26(6)? Absent the specific provisions of Section 4-5-26(6), e.g., by the South Dakota Retirement System?

3. May the standard be met by the investment in managed funds, or must the Investment Council conduct its own analysis of each venture capital investment in which the fund proposes to invest?

4. Must the Council contractually bind the venture capital fund in which it invests to comply with the prudent-man standard? Is such a fund impliedly bound to the standard?

5. Does the investment of cash flow funds in long term venture capital investments constitute an unlawful appropriation?

6. May the Investment Council invest cash flow funds in the equity of a venture capital fund?

7. May the venture capital fund in turn invest in the equities of South Dakota ventures?

IN RE QUESTION NO. 1:

The first question you raise is whether SDCL 4-5-26(6) is a valid delegation of authority pursuant to Article III, § 1 of the South Dakota Constitution.

Inherent in the division of our state government into three distinct departments by Art. II of our constitution is the principle that the Legislature cannot abdicate its essential power to enact basic policies into law, or delegate such power to any other department or body. Equally as fundamental and settled is the principle that having written broad policy into law the Legislature, in the execution of that policy, can delegate quasi-legislative power or functions to executive or administrative officers or agencies, provided it adopts understandable standards to guide its delegate in the exercise of such powers.

Boe v. Foss, 76 S.D. 295, 77 N.W.2d 1, 11 (1956).

The test to be applied in determining whether there has been a valid delegation of power by the Legislature is two-fold: (1) whether the Legislature has sufficiently expressed a will to delegate power, and (2) whether it has laid out sufficient guides or standards to guide the agency in the exercise of that power. First National Bank of Minneapolis v. Kehn Ranch, Inc., 394 N.W.2d 709, 718 (S.D. 1986); Oahe Conservancy Subdistrict v. Janklow, 308 N.W.2d 559, 563 (S.D. 1981).

A statute which grants "absolute, unregulated, and undefined discretion" in an agency is an unlawful delegation of power by the Legislature.

The presumption that an officer will not act arbitrarily but will exercise sound judgment and good faith cannot sustain a delegation of unregulated discretion.

Affiliated Distillers Brand Corp. v. Gillis, 81 S.D. 44, 130 N.W.2d 597, 600 (1964). See also, Hogen v. South Dakota State Board of Transportation, 245 N.W.2d 493, 497 (S.D.

1976); Livestock State Bank v. State Banking Commission, 80 S.D. 491, 127 N.W.2d 139, 141 (1964).

SDCL 4-5-26 provides in pertinent part:

Money made available for investment may be invested in the following classes of securities and investments and, except as provided by § 3-12-117 and the South Dakota cement plant retirement fund, not otherwise:

...

(6) Venture capital funds invested within the state of South Dakota. Such investments may not exceed five percent of the total South Dakota cash flow fund.

Subdivision (6) of this statute was added by the Legislature in 1986 by House Bill 1233, entitled "An Act to allow state investment funds to be invested in venture capital funds." S.L. 1986, Ch. 43.

In my opinion the legislative delegation of authority to the Investment Council to invest in venture capital funds is valid. There is clearly an expression of legislative will to delegate that authority. The pertinent inquiry is whether there are sufficient guides or standards which limit the agency's exercise of the discretion granted. Standing alone, SDCL 4-5-26(6) is fairly stark in the area of substantive guidelines. Only two real limits emerge. The investment must be in venture capital funds within the state, and the amount so invested may not exceed 5% of the total state cash flow fund.

When the statutory scheme is viewed as a whole, however, I am of the opinion that sufficient guidelines exist which prevent the unbridled exercise of unregulated discretion by the Council or the state investment officer. Particularly, I find that SDCL 4-5-27, which imposes a "prudent person standard" on investments applies to venture capital fund investments, and provides the requisite standards governing the agency's exercise of authority. This standard serves as a guide for not only the state investment officer, but also for the Council in promulgating rules to formulate investment policy pursuant to SDCL 4-5-28. Therefore, although the authority to invest in venture capital funds is certainly terse in terms of guidance, when read in conjunction with SDCL 4-5-27, it reflects a valid delegation of authority by the Legislature.

IN RE QUESTION NO. 2:

Your next inquiry is whether the "prudent person" standard found at SDCL 4-5-27 will permit investment in venture capital funds pursuant to SDCL 4-5-26(6). Stated in slightly different fashion, you ask whether it is ever prudent under SDCL 4-5-27 to invest funds as contemplated by SDCL 4-5-26(6). I am not prepared to state that investment in venture capital funds is per se a violation of the "prudent person" standard set forth in SDCL 4-5-27. It is an area, however, which merits a good deal of caution on the part of the Council.

SDCL 4-5-27 provides the standard against which the propriety of an investment of public funds must be measured:

Any investments under the provisions of § § 4-5-12 to 4-5-39, inclusive, shall be made with the exercise of that degree of judgment and care, under circumstances then prevailing, which persons of prudence, discretion, and intelligence exercise in the management of their own affairs, not for speculation but for investment, considering the probable safety of their capital as well as the probable income to be derived.

As your question impliedly recognizes, there is a certain degree of inherent conflict between the concept of "prudent person" investments as set forth in the statute and the concept of venture capital investment. The prudent person test requires acting not for speculation, but for investment, while weighing the safety of the capital committed against the probable gain. The concept of venture capital, on the other hand, contemplates an undertaking attended by risk and speculation through the investment of funds in a new or fresh enterprise. Typically, a venture capital investment seeks to balance the higher degree of risk against the potential for a higher return on the investment.

Notwithstanding this philosophical conflict, it seems clear that the Legislature intended to authorize investment in activities with a higher degree of risk than the other types of investments permitted in the first five subdivisions of SDCL 4-5-26. I do not doubt the authority of the Legislature to do so, and the wisdom of doing so is solely a matter for the Legislature. Clem v. City of Yankton, 83 S.D. 386, 160 N.W.2d 125 (1968). It is not permissible to assume that they did not realize the implications of what they authorized. The prudent person statute was adopted by the Legislature in 1971 when the major portion of the statutes creating the State Investment Council were passed. The content of the statute has remained essentially the same, and it must be presumed that the

Legislature was cognizant of this investment standard when it adopted SDCL 4-5-26(6). State v. Feiok, 365 N.W.2d 536 (S.D. 1985).

Only when two statutes are so repugnant to each other as to render it impossible to harmonize them must one give way. Admittedly it is possible to argue that SDCL 4-5-26(6) is so contradictory to SDCL 4-5-27 that it is not possible to reconcile the two statutes. That is a result, however, which courts have traditionally avoided when attempting to determine legislative intent.

Rules of statutory construction require that meaning be given to both provisions, and that they be interpreted in a manner which avoids the conflict, if that can be done without violating the intent of the Legislature, or the Constitution. See Meyerink v. Northwestern Public Service Co, 391 N.W.2d 180 (S.D. 1986).

Thus I am not able to conclude that venture capital investments made pursuant to SDCL 4-5-26(6) are per se imprudent under SDCL 4-5-27. To do so would render SDCL 4-5-26(6) a nullity, a result which is not permissible if a reasonable accommodation between the statutes is possible.

Determining a reasonable accommodation requires examination of the burden SDCL 4-5-27 places on the Council and the investment officer. Not coincidentally, the standard imposed on investments pursuant to SDCL 4-5-27 is the same as the standard imposed upon fiduciaries generally in dealing with property for the benefit of another. See SDCL 55-5-1. Accordingly, in my opinion SDCL 4-5-27 makes clear that the Council and investment officer are regarded as trustees of the funds invested, and should approach the investment decisions in light of the fiduciary responsibility to the beneficiaries of the funds. SDCL 4-5-29 further reflects that position by requiring the investment officer "to see that moneys invested ... are at all times handled in the best interests of the state." See generally, 63A Am.Jur.2d, Public Funds, § 2 at 393; 63A Am.Jur.2d, Public Officer and Employees, § 348, at 919-20.

It is important to keep in mind, however, that many courts have concluded that a public officer is held to a much stricter standard of liability than fiduciaries handling private funds. Those courts have concluded that public officials are absolutely liable as an insurer for the safekeeping of funds and are liable for losses which occur even without fault. See, e.g., Bordy v. Smith, 150 Neb 272, 34 N.W.2d 331 (1948); Northern Pacific Ry. Co. v. Owens, 86 Minn 188, 90 N.W. 371 (1902). Still other courts have concluded that there is

not absolute liability, and regard a public officer as a trustee who is liable only if he fails to exercise good faith, diligence, prudence, caution and a disinterested effort to keep and preserve the funds. See generally, 63A Am.Jur.2d, Public Officer and Employees, § 394, at 955-56.

It is not clear which judicial philosophy our courts would follow. Most South Dakota case law on the subject deals with the use and investment of the permanent school fund and other educational funds held in trust pursuant to specific provisions of Article VIII of the state constitution. The Court has referred many times to "the sacred character of this important trust" and has struck down several attempts at creative use of the funds. State v. Ruth, 9 S.D. 84, 68 N.W. 189, 190 (1896); Schomer v. Scott, 65 S.D. 353, 274 N.W. 556 (1937); Schelle v. Foss, 76 S.D. 620, 83 N.W.2d 847 (1957). The language of Art. VIII, § 13, appears to create liability for "defalcation, negligence, mismanagement or fraud," and State v. Ruth, supra tends to support such an approach. Compare Merkwan v. State of South Dakota, 375 N.W.2d 624 (S.D. 1985).

In a more general setting, our court has concluded that a treasurer of a school district is a trustee, and would be liable for a breach of duty under common law principles and statute for losses occasioned by putting school district funds in a bank he knew to be failing. Independent School District of City of Brookings v. Flittie, 223 N.W. 728 (S.D. 1929). "That some one other than the treasurer is intrusted with the duty of designating a depository certainly does not discharge the treasurer from all obligations of good faith and common honesty in connection with the performance of his trust." 223 N.W. at 730. The reasoning employed in this case would support the argument that public officers are not insurers of moneys in their custody, but rather are liable only upon proof of a lack of good faith, failure to exercise prudent judgement, or something more serious, like fraud.

Similarly, in the case of a fiduciary of private funds the court has held:

The law is well established in this state that the deposit of trust funds in a bank by a trustee who knows the bank is insolvent, constitutes a breach of duty by the trustee and renders the trustee liable for any resulting loss. In re Hogness' Guardianship, 56 S.D. 286, 228 N.W. 379; In re Taylor's Estate, 58 S.D. 365, 236 N.W. 365; Onida Independent School District No. 1 v. Groth et al., 53 S.D. 458, 221 N.W. 49; Independent School District of Lake Andes v. Scott et al., 51 S.D. 187, 212 N.W. 863; Independent School District of City of Brookings v. Flittie et al., 54 S.D. 526, 223 N.W. 728.

In Re Fisher's Estate, 4 N.W.2d 797, 800 (S.D. 1942). Again, the basis of the conclusion is that it is the breach of a duty which imposes the liability. That rationale appears to be consistent with the general rules for imposing liability on a trustee, as stated in SDCL ch. 55-2. For example, SDCL 55-2-10 provides:

A trustee who uses or disposes of the trust property in any manner not authorized by the trust but in good faith and with intent to serve the interest of the beneficiary is liable only to make good whatever is lost to the beneficiary by his error.

The general obligation of good faith is stated as follows:

A trustee must act in good faith in the administration of the trust, and this requirement means that he must act honestly and with finest and undivided loyalty to the trust, not merely with that standard of honor required of men dealing at arm's length in the workaday world, but with a punctilio of honor the most sensitive. He must act with such high good faith in the exercise of any discretion vested in him, in the use of judgment and the making of decisions in the administration of the trust, and in the investigation and determination of facts as a basis for his judgment and decisions.... The liberality with respect to a trustee of provisions in a trust instrument or declaration in no way diminishes the trustee's duty to act in utmost good faith.

73 Am.Jur.2d, Trusts, § 315, at 534. A failure to meet the standard of care renders the trustee liable for all losses resulting to the trust estate. It is against this backdrop that you must examine the prudence of a venture capital investment.

Perhaps the most troublesome duty which the prudent person standard places on the Council is found in the language dealing with speculation.

It is generally agreed that under the general rule of requisite care, diligence, and skill as applied to trust investments, a trustee is not authorized to make or retain trust investments that are speculative, even where they are of such promise and character that a prudent person might make them for himself. The reasons for the application of the rule to exclude such speculation are as follows: (1) The ordinarily prudent man, apart from any question of legal liability, will act with greater concern for the safety of funds where he is handling them in a fiduciary capacity than where they are his own funds; (2) public policy and the law contemplate that an ordinarily prudent man acting in a fiduciary capacity will, even apart from any question of legal liability, act with great tenderness for the safety of money that he is investing; and (3) the object of the trust is primarily safety of, and secondarily income from, the trust estate, so that the situation is comparable to that of a man of

ordinary prudence seeking a permanent, safe, and income-producing disposition of the funds, rather than a greater than ordinary income.

76 Am.Jur.2d, Trusts, § 420, at 638-39. As your request indicates, however, the basic idea behind venture capital investment is to a large extent speculation. Thus you are faced with a fiduciary duty not to speculate and a legislative authorization allowing speculation.

The situation is analogous to a trustee receiving specific authorization from the creator of the trust to invest in nonlegal investments. Here the trust instrument, the statute, provides the trustee with the discretion to make an investment which otherwise could not have been made absent that grant of authority. Such an authorization is to be strictly construed, but if it exists, the trustee is still obligated to act in good faith, with the requisite care, diligence and skill of a prudent person under similar circumstances. The authorization to make such an investment, therefore, does not mean all such investments are prudent. You must bear in mind that the burden will probably be on you to show the prudence of an investment in order to protect yourself from liability resulting from the loss therefrom.

It is not possible to categorize prudent behavior on a general basis. The prudent person determination is going to have to be made on a case-by-case basis. It seems to me, however, that in making that determination it will be important to keep in mind the nature of the asset being invested. Here you will be working with the "cash flow fund." Although this is not one of the funds specifically enumerated in SDCL 4-4-4, I assume it is a readily identifiable fund. Whatever else can be said about the composition or identity of the fund, it seems clear that it consists of moneys which have been appropriated by the legislature for specified purposes unrelated to venture capital investments. I would also assume that the source of the moneys that compose the fund is constantly changing. While I realize that the balance of such a fund is probably fairly constant, the ever changing nature of its composition seems to me to dictate a need for an investment which is fairly short term and very liquid. Also the fact that the Legislature has already appropriated these funds for other purposes seems to dictate that special attention be given to the safety of the funds. The nature of the asset would also seem to call for diversification of investment even within the venture capital setting, something which your rules already require.

As compared to other investments the Council and investment office make, this type of investment seems to present a more tangible possibility of loss of assets, as opposed to a risk of poor return on investment. It seems that you will have to carefully weigh the impact of such a potential loss on the state budget as funded.

Thus, while I do not conclude that investment in venture capital funds pursuant to SDCL 4-5-26(6) is imprudent per se, I am of the opinion that you will have to proceed with great care should you choose to exercise the investment discretion granted. It may be advisable to examine the possibility of developing some further criteria in your rules to serve as a guide in determining which venture capital funds constitute an acceptable risk. In the final analysis, however, prudence will have to be examined under the peculiar facts of each case.

The second portion of your question deals with venture capital investments by the South Dakota Retirement System. While SDCL 3-12-117 indicates that the Council has more flexibility in investing retirement funds, that statute also points out that SDCL 4-5-27 also applies in this setting. Obviously, different factors will have to be considered in making a determination as to the prudence of an investment, because the nature of the asset is different. These funds are not otherwise appropriated for the fiscal year. The need for liquidity may not be as great, and a longer term seems possible. You should keep in mind, however, that the fiduciary responsibility remains the same, and careful consideration will have to be given to the safety of the investment.

IN RE QUESTION NO. 3:

The "prudent person" standard is not satisfied simply by meeting the standard in the initial investment decision. Assuming that the initial investment in a venture capital fund was prudent when done, that does not relieve the Council or the investment officer of the obligation to ensure that the investment remains a prudent one. In short, the obligation imposed by the statute, SDCL 4-5-27 is a continuing one--what is prudent today may not be prudent tomorrow.

In my opinion, you will have to continue to monitor an investment once it has been made to satisfy yourself that it remains a prudent investment of funds. That should include an examination of how the venture capital funds are using the moneys you have invested. See Independent School District of City of Brookings v. Flittie, supra; In Re Fisher's Estate, supra. I do not believe it is permissible to pass on your duty of prudent investment to the manager of a private fund. Neither are you relieved of the obligation to continue to keep advised regarding the continued prudence of the investment. That does not mean you must be or should be actively involved in managing the venture capital fund. It does mean you should actively monitor the use of the investment by the fund, and should take appropriate action to protect your investment should the use of the money cause you to believe the investment is no longer a prudent one.

IN RE QUESTION NO. 4:

You further ask whether the Council must bind a venture capital fund to comply with the "prudent person" standard, or whether such a fund is impliedly bound by the standard, in utilizing the moneys invested. In my opinion the answer to both parts of the question is NO.

SDCL 4-5-27 imposes the "prudent person" standard on the Council and the investment officer, not the entity which receives the funds invested. While the manner in which the venture capital fund utilizes the moneys invested would be continuously monitored by the Council and investment officer to determine whether the investment remains prudent, the venture capital fund itself would not be subject to SDCL 4-5-27. (Although it is possible that a venture capital fund is a trust with its own fiduciary responsibility, that strikes me as unlikely.)

IN RE QUESTION NO. 5:

Your fifth question raises the issue of whether investing cash flow funds in venture capital on a long term basis constitutes an unlawful appropriation of funds. Assuming for the sake of argument that long term investment in venture capital funds is prudent, it is my opinion that SDCL 4-5-26(6) is not an appropriation.

Article XII, § 1 of the South Dakota Constitution provides that "[n]o money shall be paid out of the treasury except upon appropriation by law ... " SDCL 4-8-1 provides:

All expenditures of the state and of its budget units of moneys drawn from the state treasury shall be made under the authority of appropriation acts, which shall be based upon a budget as provided by law, and no money shall be drawn from the treasury, except by appropriation made by law pursuant to article XII, section 2, Constitution of the state of South Dakota.

SDCL 4-7-1(1) defines an "Appropriation" as follows:

An authorization by the Legislature to a budget unit to expend, from public funds, a sum of money not in excess of the sum specified, for the purposes specified in the authorization and under the procedure described in this chapter.

Our state Supreme Court considered the definition of the term appropriation in State ex rel. Parker v. Youngquist, 11 N.W.2d 84 (S.D. 1943) and held:

An appropriation is legislative sanction for the disbursement of the public revenue.... The test of whether an act is an appropriation is whether the money may be paid or drawn from the state treasury on authority of the act.... The act in question authorizes no disbursement of public revenue. No money may be drawn from the state treasury on authority of the act.... This law is not an appropriation of public money.

11 N.W.2d at 86 (citations omitted)

Here, the authorization from the Legislature is to invest public funds, not expend them. Indeed, the funds authorized for investment have already by in large been appropriated for specific purposes. That an investment may be lost, and the funds thereby removed from the treasury does not make every investment an expenditure which requires an appropriation. Logic dictates that SDCL 4-5-27 was designed to minimize the possibility of such a loss. Although an investment may temporarily make funds unavailable for other uses, it does not constitute an expenditure. While the length of time the money is invested may raise questions concerning the prudence of the investment, a long term investment does not automatically become an expenditure. My answer to your fifth question is NO.

IN RE QUESTION NO. 6:

Your next question is whether the Investment Council may invest cash flow funds in the equity of a venture capital fund. In my opinion, such an investment is not permitted under Article XIII, § 1 of the South Dakota Constitution.

S.D.Const.Art. XIII, § 1 provides in part:

For the purpose of developing the resources and improving the economic facilities of South Dakota, the state may engage in works of internal improvement, may own and conduct proper business enterprises, may loan or give its credit to, or in aid of, any association or corporation, organized for such purposes. But any such association or corporation shall be subject to regulation and control by the state as may be provided by law. No money of the state shall be appropriated, or indebtedness incurred for any of the purposes of this section, except by the vote of two-thirds of the members of each branch of the Legislature.

Admittedly, the reach of that language is broad. After Clem v. City of Yankton, 83 S.D. 386, 160 N.W.2d 125 (1968) there should be little doubt that the policy of assisting economic development is a public purpose. See also Meierhenry v. City of Huron, 354 N.W.2d 171 (S.D. 1984). However, the constitutional language must still be observed, and the particular act must still be examined to determine its public purpose.

Of critical importance to the inquiry is the 1936 amendment to Article XIII, § 1. Prior to that amendment, Article XIII, § 1 provided:

For the purpose of developing the resources and improving the economic facilities of South Dakota, the state may engage in works of internal improvement, may own and conduct proper business enterprises, may loan or give its credit to, or in aid of, any association, or corporation, and may become the owner of the capital stock of corporations, organized for such purposes ... (emphasis added).

The 1936 amendment, among other things, deleted the grant of authority for the state to own stock in corporations. While the general rule is that the Constitution is a limitation on the Legislature, and it is possible to argue that there is no prohibition on the state owning an equity interest in a business, I find it significant that the state once had such power, and it was withdrawn by the people.

Usually amendments are adopted for the express purpose of making a change in the existing system. Particularly applicable in the case of amendments are the rules relating to the intent of the framers and adopters and attainment of the object of a constitution. "The courts are under the duty to consider the old law, the mischief, and the remedy, and to interpret the constitution broadly to accomplish the manifest purpose of the amendment." 16 Am.Jr.2d Constitutional Law § 88 at 415 (1979) (footnotes omitted). This court followed this mandate in State v. Reeves, 44 S.D. 568, 184 N.W. 993 (1921).

'Generally speaking, principles of construction applicable to statutes are also applicable to constitutions, but not to the extent of defeating the purposes for which a constitution is drawn.' Egbert v. City of Dunseith, 74 N.D. 1, 6, 24 N.W.2d 907, 909 (1946).

South Dakota Auto. Club v. Volk, 305 N.W.2d 693, 697 (1981). See also, Rosander v. Board of County Commissioners of Butte County, 336 N.W.2d 160 (S.D. 1983); Hot Springs Independent School Dist. No. 10 v. Fall River Landowner's Association, 262 N.W.2d 33 (S.D. 1978); State v. Heisinger, 252 N.W.2d 899 (S.D. 1977).

Viewing the 1936 amendment in that light, and in conjunction with the other provision of the amendment limiting county rural credit loans, it appears to me that the people of South Dakota intended to deny the State the power to own stock in a corporation. Further, the language of Article XIII, § 1 allows the State to 1) engage in works of internal improvement; 2) own and conduct proper business enterprises; and 3) "loan or give its credit to, or in aid of, any association, or corporation," organized "[f]or the purpose of developing the resources and improving the economic facilities of South Dakota." The

proposed use of the funds here is certainly not a work of internal improvement; neither has it been proposed that the State own a business enterprise. Therefore, the State is restricted to loaning or giving its credit to or in aid of a business which improves the economic facilities of the State. In my opinion, the direct investment in an equity position is not permissible.

While I am cognizant of the difficulties this interpretation presents in terms of the practicalities of the investment world, I do not believe the Legislature can exercise a power the people have specifically withdrawn simply by passing a statute. Although SDCL 4-5-26(6) is on its face broad enough to permit equity type investments, the 1936 constitutional amendment prevents me from according the language of the statute that meaning. My answer to your sixth question is NO.

IN RE QUESTION NO. 7:

Your final question is whether the venture capital fund, utilizing the money invested by the Council, is permitted to make equity investments in South Dakota ventures. The constitutional limitation discussed in question 6, above, applies to the State, not to private entities. Unless the Council chooses by regulation or agreement to limit the manner in which venture capital fund may utilize the funds invested, I find no statute related to investment of state public funds that would restrict how the venture capital fund may use the investment. This assumes of course that the Council has examined the proposed use and determined that the investment by the Council is prudent under SDCL 4-5-27. My answer to your seventh question is YES.

Respectfully submitted,

Roger A. Tellinghuisen
Attorney General