

OFFICIAL OPINION NO. 89-31, Investment of public funds in securities directly or indirectly guaranteed by the United States Government

November 1, 1989

Maurice Christiansen, Auditor General
Department of Legislative Audit
435 S. Chapelle
Pierre, South Dakota 57501

OFFICIAL OPINION NO. 89-31

Investment of public funds in securities directly or indirectly guaranteed by the United States Government

Dear Mr. Christiansen:

You have requested an official opinion from this Office based upon the following factual situation:

FACTS:

In 1987, I requested an official opinion relating to the investment of public funds in securities directly or indirectly guaranteed by the United States Government. In Official Opinion No. 87-06 you responded to this question in part by stating that local government subdivisions under South Dakota law could not invest in "government" mutual funds. In an apparent response to your opinion, the South Dakota Legislature amended SDCL 4-5-6 in 1988 in part to specifically authorize local governmental subdivisions to invest in open-end, no-load funds whose only assets are repurchase agreements collateralized by, or securities issued or directly or indirectly guaranteed by the United States government. Since SDCL 4-5-6 was amended, a number of local governmental entities, investment companies and other entities have been asking which types of mutual funds are legal investments. Certain mutual funds have been referred to as "government" mutual funds because their asset listing is comprised solely of government securities. There are, however, a wide range of government securities, some of which are backed by the full faith and credit of the United States government, some are supported by the right of the issuer to borrow from the United States treasury and some are supported only by the credit of the federal agency or instrumentality.

Based upon the above facts, you have asked the following question:

QUESTION:

What is the definition of "directly or indirectly guaranteed by the United States government" as it is used in SDCL 4-5-6 as amended?

IN RE QUESTION:

SDCL 4-5-6 as amended in 1988 now provides:

Any public funds which will not be needed for current operating expenses may be invested in: (a) securities of the United States and securities guaranteed by the United States government either directly or indirectly including, without limitation, United States treasury bills, notes, bonds and other obligations issued or directly or indirectly guaranteed by the United States government, or otherwise directly or indirectly backed by the full faith and credit of the United States government; provided that, for other than permanent, trust, retirement and building funds, such securities shall either mature within eighteen months from the date of purchase or be redeemable at the option of the holder within eighteen months from the date of purchase; or (b) repurchase agreements fully collateralized by securities described in (a) and meeting the requirements of section 4-5-9, if the repurchase agreements are entered into only with those primary reporting dealers that report to the federal reserve bank of New York and with the one hundred largest United States commercial banks, as measured by domestic deposits; or (c) in shares of an open-end, no-load fund administered by an investment company registered under the Federal Investment Company Act of 1940, whose shares are registered under the Federal Securities Act of 1933 and whose only investments are in securities described in (a) and repurchase agreements described in (b).

The 1988 Amendments authorized investment in certain types of mutual funds and repurchase agreements. Though the 1988 Amendments broadened the scope of authorized investments, the Legislature did not modify the types of United States governmental securities in which a local governmental entity may invest. Only securities issued and directly or indirectly guaranteed are authorized. As such, Official Opinion No. 87-06 is still applicable in this matter. In that Official Opinion, I stated:

"[S]ecurities guaranteed by the United States Government, either directly or indirectly," would include bonds, notes and other securities for which the United States Government will guarantee payment if the obligor fails to perform his responsibilities. Examples of these types of securities would include G.N.M.A.s and F.R.M.A.C.s and other comparable types of securities.

In an attempt to further clarify what constitutes direct or indirect guarantees, it is my opinion that any securities issued by governmental agencies or instrumentalities that are backed by the full faith credit of the United States; are general obligations of the United States; or whose repayment of principal and interest are assured by a federal agency or instrumentality may be purchased. In my opinion, the South Dakota Legislature in using the phrase "directly or indirectly" meant more than the fact that the securities were guaranteed by the full faith and credit of the United States Government. In my opinion, the Legislature intended to authorize investment in securities which the federal government is contractually or legally obligated to make payment of interest and principal.

In order to make a determination regarding whether a particular security falls within the directly or indirectly guaranteed portion of SDCL 4-5-6 the applicable federal legislation, agency rules and actual prospectus should be reviewed. Given the wide variety of obligations, it is impossible for me to provide a list of specific securities that can be purchased by local governmental entities through direct purchase, or through purchase of an open-end no-load mutual fund or a repurchase agreement. A local governmental entity that is purchasing the securities, repurchase agreement or no-load mutual fund is required to have sufficient information available to justify the purchase of securities it claims fall within SDCL 4-5-6 provisions.

Respectfully submitted,

ROGER A. TELLINGHUISEN
ATTORNEY GENERAL

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