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**To:** Susan D. Battani, CPA  
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**From:** Christie J. Scase *C. Scase*  
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**Date:** April 22, 2008

**Re:** Transfer of public funds to private non-profit organization

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You have requested my advice regarding the disposition of gifts received by governmental entities. You explain that governmental agencies periodically receive gifts from individuals either through bequest or other means. Such gifts are often given with a stipulation that the funds or property be used for a specific purpose or purposes. We have recently discussed two separate situations in which testators willed funds to a city library or to a city to be used for library purposes and, upon receipt of the bequests, the city library board of trustees transferred the gifts to local nonprofit foundations.

In one case, in excess of \$ 1,000,000.00 was received and immediately transferred by the library board to a local private nonprofit foundation to form an endowment. According to the foundation's audited financial statement for the year ended June 30, 2006: the foundation was formed to raise funds to benefit the city public library; cash and certificates of deposits are maintained at several financial institutions and at times may exceed federally insured limits; and a majority of the foundation's net assets are invested in marketable securities. In the other case, approximately \$ 250,000.00 was bequeathed to a city to be used to "purchase books, periodicals and journals." The funds were given by the library board to a local private nonprofit foundation which serves a broad range of educational and charitable interests. At this time you do not know if the foundation has earmarked the funds received from the library board so that it can demonstrate compliance with the terms of the bequest.

In light of this background, you ask whether gifts received from private donors by a governmental body may be given by the governmental body to a private non-profit organization and, if so, whether the private non-profit organization must adhere to the terms of the gift and statutory requirements governing the deposit and investment of public funds found in Iowa Code

chapters 12B and 12C. It is my view that a governmental body may not simply donate funds received from private donors to a private non-profit organization, even if the organization intends to use the funds for the same purpose for which they were given to the governmental body. Although a governmental body can not irrevocably transfer public funds to a private non-profit organization, it can enter into a true joint or cooperative undertaking with a private agency under Iowa Code section 28E.4, as long as the government body retains the ability to oversee and control expenditure of the funds and ensures that use of the funds complies with any restrictions placed upon use of the gift and that the funds are managed in a manner consistent with the limitations on the deposit and investment of public funds contained in Code chapters 12B and 12C.

Past opinions of this office have consistently concluded that a governmental body may not *donate* public funds to a private entity, even if the entity is established for charitable or educational purposes and performs work which the government could perform directly. See Iowa Op. Att’yGen. #00-8-2(L) (Kempkes to Bjomstad) [2000 WL 1576488] (concluding court might void transfer of funds by county board of supervisors to nonprofit organization created to serve as advisory group to county conservation board); 1990 Iowa Op. Att’yGen. 10 (#89-2-6(L)) [1989 WL 264884] (county hospital board may not transfer assets to a foundation if the effect is to deprive future boards of trustees of control over hospital assets); 1980 Iowa Op. Att’yGen. 701 (#80-5-7(L)) [1980 WL 25979] (county could not make appropriation to be used by private nonprofit historical society to construct building to house museum); 1978 Iowa Op. 369 (#78-1-3) [1978 WL 17335] (board of regents lacked authority to transfer funds to a non-profit foundation the board was statutorily authorized to create for the support of the institutions governed by the board); 1976 Iowa Op. Att’yGen. 31 (#75-2-2) (board of trustees of a municipal utility could not donate city funds to a private hospital clinic); 1976 Iowa Op. Att’yGen. 634 (#76-7-11) (city hospital could not directly contribute funds to a private corporation for purposes of providing medical education and clinic services within another city in the county); 1972 Iowa Op. Att’yGen. 395 (#72-3-16) (city council could not make a donation from city funds to a recreation center operated by private citizens). These opinions are based upon several legal principles.

Public nature of the fund: As you note in your letter to me, private gifts and bequests of money to a city or county, upon receipt and acceptance, “become public funds under the stewardship of the [city or] county.” Op. #00-8-2(L) at p. 2, citing 10 E. McQuillan, *The Law of Municipal Corporations*, § 28.15, at 39-40 (1999). In addition to any restrictions or limitations imposed by the donor on use of the funds, all of the constitutional and statutory requirements regarding accounting for, depositing, investing, and expending public funds apply equally to funds received through taxation and funds received from private donors. “To paraphrase an earlier opinion, ‘What cannot be lawfully done by a public agency cannot be delegated to a private entity.’” Op. #00-8-2(L) at p. 4, citing 1988 Iowa Op. Att’yGen. 112 (#88-10-2(L)) [1988 WL 247803] and 15 E. McQuillan, *The Law of Municipal Corporations*, § 39.47, at 164 (1995) (legislature may regulate the holding of public funds and local ordinance cannot change such regulation).

Political subdivisions and municipalities, including cities, counties, schools, and townships are municipal – governmental – entities. As governmental entities they are governed by elected bodies, are directly responsible to the public as a whole, and are subject to the limitations imposed on them by the state. Although a private organization may be formed to provide and support “public” services which are the same or similar to the services provided by government, the private organizations are not subjected to the same degree of public accountability and oversight as governmental entities. Whether a gift or bequest intended to support public services will be subject to the control of a government agency or a private organization is a choice made by the donor. A private donor can choose to leave gifts of money to a governmental entity or to a private organization. When a donor opts to give a monetary gift to a governmental entity, the funds become public funds and the governmental body receiving the funds must account for the deposit, investment, and expenditure of the funds.

Public purpose: The Iowa Constitution prohibits governmental bodies from making a gift to a private non-profit corporation. Article III, section 31 states: “No public money or property shall be appropriated for local, or private purposes, unless such appropriation, compensation, or claim, be allowed by two thirds of the members elected to each branch of the General Assembly.” This provision has been found by the Iowa Supreme Court to be applicable to appropriations by city councils. 1986 Iowa Op. Att’yGen. 113 (#86-8-8) [1986 WL 79961], citing Love v. City of Des Moines, 210 Iowa 90, 101, 230 N.W. 373, 278 (1930); Willis v. City of Des Moines, 357 N.W.2d 567, 570, 572 (Iowa 1984).

Even if the function of a private non-profit corporation fits within the scope of activities generally recognized as serving a public purpose, a critical question exists regarding whether funds or property transferred to a private entity will indeed be used for those public purposes. If adequate oversight provisions are included, a transfer of funds or property to a private non-profit entity may be allowable. See Iowa Op. Att’yGen. #98-1-3 [1998 WL 213719] (addressing restrictions placed upon use of fund transferred to non-profit Iowa Housing Corporation by the Iowa Finance Authority); 1996 Iowa Op. Att’yGen. 38, #95-10-1 [1995 WL 792842] (finding that a lease for ten dollars per year by city to a private non-profit corporation was not prohibited gift because the lease provisions required the corporation to provide health care services, to maintain the property, to provide services in consideration of the lease to the city, and provided for reversion of the property to the city upon termination of the lease); 1980 Iowa Op. Att’yGen. 701 (#80-5-7(L)) [1980 WL 25979] (concluding that a county could appropriate money to support a private historical society only upon conditions that assured that the property would continue to be used for the public purpose). Code chapter 28E authorizes a wide range of joint or cooperative public and private undertakings, but imposes significant public accountability measures to ensure that public funds contributed to the undertaking are used for the intended public purposes. Iowa Code §§ 28E.4, 28E.5, 28E.7 (2007); Iowa Code Supp. §§ 28E.6, 28E.8 (2007); see Goreham v. Des Moines Metropolitan Area Solid Waste Authority, 179 N.W.2d 449, 455 (Iowa 1970) (“The creation of a new body corporate and politic to jointly exercise and perform the duties and responsibilities of the cooperating governmental unit would not be unconstitutional so long as the new body politic is doing only what its cooperating members

already have the power to do.”); Iowa Op. Att’yGen. #98-1-3 [1998 WL 213719]; 1976 Iowa Op. Att’yGen. 634, 636 (#76-7-11); (“Section 28E.4 provides that any public agency may enter into an agreement with a private agency for joint or cooperative action pursuant to that chapter. . . . However, the city should have a hand in the management of the action and should received some benefit from it.”).

As the 1998 opinion concluded it is not *per se* unlawful to transfer public funds to a private entity, if adequate safeguards are built into the transaction. In the absence of adequate safeguards, a pure gift or donation to a private entity will not meet the public purpose requirements of Iowa law.

Delegation of control: The transfer of public funds to a private non-profit corporation also raises concerns regarding the delegation of the discretion of the governing body of the government entity over the use and expenditure of the funds. The cases underlying your inquiry each involve funds given to cities for support of the city libraries. Assuming, for purposes of this advice, that the libraries are established as city administrative agencies under Code chapter 392, they are governed by a library board of trustees.<sup>1</sup> The library trustees are explicitly authorized to “accept and control the expenditure of all gifts, devises, and bequests to the library.” Iowa Code § 392.5 (2007).<sup>2</sup> Control of library assets, including funds received by gift or bequest, is a duty of the board of trustees. They may not turn over future control of library assets to a private foundation to administer and control. As we stated with regard to a transfer of county hospital funds to a private foundation for the purpose of providing health care scholarships, “because control of the hospital assets was a duty of the hospital board and the exercise of a government function, the current board lacked authority to bind future board from

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<sup>1</sup> Iowa Code section 392.5 provides that “[a] city library board of trustees functioning on the effective date of the city code shall continue to function in the same manner until altered or discontinued” upon approval of the voters of the city. Iowa Code § 392.5 (2007), as enacted by 1972 Iowa Acts, 64<sup>th</sup> G.A., ch. 1088, § 196 (pursuant to section 9 of the act, this provision was effective July 1, 1972, if adopted by resolution of city council, otherwise effective July 1, 1974).

<sup>2</sup> In many cases, city ordinances incorporate the functions afforded library boards under the statutes existing in 1972, as contemplated by the transition provisions in that act. These statutes vested control over budgeting and the allocation and spending of library funds with the board of trustees. Iowa Code § 378.10(8) (1973) (the “board of library trustees shall have and exercise the following powers: . . . [t]o have exclusive control of the expenditures of all portions of the municipal enterprises fund allocated for library purposes by the council, and of the expenditure of all moneys available by gift or otherwise for the erection of library buildings, and of all other moneys belonging to the library fund, including fines and rentals collected under the rules of the board of trustees”), see also Iowa Code § 378.10(5) (1973) (empowering the board of library trustees to “select and make purchases of books, pamphlets, magazines, periodicals, papers, maps, journals, furniture, fixtures, stationery, and supplies for [the] library”).

controlling these assets by placing them in a foundation.” 1990 Iowa Op. Att’yGen. 10 (#89-2-6(L)) [1989 WL 264884]; see also Iowa Op. Att’yGen. #98-1-3 [1998 WL 213719].

Donor restrictions: “It is well established that the donor of [a] gift may impress upon [the] gift such conditions and limitations as the donor sees fit.” 1972 Iowa Op. Att’yGen. 303 (#71-11-21) (addressing school board obligation to comply with restrictions imposed by donor of gift to school district); see also 1986 Iowa Op. Att’yGen. 134 (#86-12-13) [1986 WL 79966]. With the statutory authority to accept and expend gifts afforded to library trustees comes the responsibility to ensure that the proceeds of the gift are spent in a manner consistent with any restrictions places upon use of the gift by the donor. 1972 Iowa Op. Att’y Gen. at p. 304 (“The funds must be earmarked and spent for the purpose for which the gift was made.”).

Deposit and investment restrictions: The statutory restrictions upon the deposit and investment of public funds act as a further barrier to the unrestricted donation of public funds to a private foundation. This office most recently addressed issues regarding the transfer of public funds to a private nonprofit corporation in an opinion addressing gifts received by a county to be used for conservation purposes. Iowa Op. Att’yGen. #00-8-2(L) [2000 WL 1576488] (copy attached). In that opinion we were asked whether a county board of supervisors could directly transfer money given by private donors for conservation purposes to a nonprofit organization which would use the funds for substantially the same functions as the county conservation board, but would invest the money in ways the county could not lawfully invest it. This opinion focused primarily upon the statutory provisions found in Code chapters 12B and 12C, which regulate the deposit and investment of public funds held by political subdivisions. As we stated, these statutes are part of

“a long standing state scheme [which] restricts the investment authority of counties and other political subdivisions.” 1988 Op. Att’yGen. 87, 88 (#88-4-5) [1988 WL 247774]. The investment options available under this state scheme can be fairly describes as conservative in nature and protective of principal. See generally Iowa Code chs. 12B, 12C. Although these investments normally generate a relatively low rate of return, they further a presumably more important legislative purpose: guarding against a loss, great or small, of public funds.

Iowa Op. Att’yGen. #00-8-2(L) at p. 3.

Code section 384.20 provides, in relevant part, that each “[c]ity shall keep accounts which show an accurate and detailed statement of all public funds collected, received, or expended for any city purpose, by any city officer, employee, or other person , and which show the receipt, use, and disposition of all city property.” Iowa Code § 384.20 (2007) (unnumbered par. 2). “A city may establish trust and agency funds for the [purpose of] . . . accounting for gifts received by the city for a particular purpose.” Iowa Code § 384.6(2) (2007). Cities are directed

to “keep all funds invested to the extent practicable and may invest the funds jointly with one or more cities” or other listed government entities. Iowa Code § 384.21 (2007). However, “[a]ll investments of funds shall be subject to sections 12B.10 and 12B.10A and other applicable law.” Id.

Code section 12B.10 establishes investment standards applicable to public funds held by political subdivisions.

2. . . . political subdivisions of the state, when investing or depositing public funds, shall exercise the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use to attain the goals of this subsection. This standard requires that when making investment decisions, a public entity shall consider the role that the investment or deposit plays within the portfolio of assets of the public entity and the goals of this subsection. The primary goals of investment prudence shall be based in the following order of priority:

- a. Safety of principle is the first priority.
- b. Maintaining the necessary liquidity to match expected liabilities is the second priority.
- c. Obtaining a reasonable return is the third priority.

3. Investments of public funds shall be made in accordance with written policies. A written investment policy shall address the goals set out in subsection 2 and shall also address, but is not limited to, compliance with state law, diversification, maturity, quality, and capability of investment management.

The trading of securities in which any public funds are invested for the purpose of speculation and the realization of short-term trading profits is prohibited.

Iowa Code § 12B.10(2), (3) (2007). Political subdivisions of the state may purchase and invest in only the types of investments which are listed within subsection 12B.10(5). Similar parameters for the deposit of public funds, designed to prevent “the loss of public funds on deposit in a depository” are set forth in Code chapter 12C. Iowa Code § 12C.1(4) (2007).

The deposit and investment standards carefully defined within chapters 12B and 12C, could be readily circumvented if a governmental body was allowed to give public funds to a private nonprofit corporation, which in turn were not subject to the standards.

Investment of public funds must strictly follow legislative commands, 63C Am. Jur. 2d *Public Funds* §§ 5, at 229 (1997), and a court, mindful of the public protections underlying chapter 12C, would likely scrutinize such a direct transfer to a county's apparent alter ego, see 1998 Op. Att'y Gen. \_\_\_ (#98- 1-3); see also 1980 Op. Att'y Gen. 317 (#79-8-2(L)) (quasi-state agencies "may often find themselves bound by restrictions prescribed in laws affecting state agencies"). Cf. Dyer v. City of Des Moines, 230 Iowa 1246, 300 N.W. 562, 566 (1941) (city forced to take custody of funds possessed by private entity, who, on city's behalf, collected fees for automobile testing and placed them in bank of its own choice: such city-owned funds must be "handled in the same manner as in which all other funds of the city are handled"). We point out that public funds do not necessarily lose their public character merely because a private entity happens to possess them. See 1994 Op. Att'y Gen. 71 (#93- 12-3(L)); see also 1998 Op. Att'y Gen. \_\_\_ (#98-1-3).

Iowa Op. Att'yGen. #00-8-2(L) at p. 4. We concluded with regard the county conservation funds at issue in the 2000 opinion, "[a] court might void a county's direct transfer of county-owned funds to a nonprofit organization that, in addition to expending them on the county's behalf, would invest them in ways the county could not lawfully invest them." Id. at p. 5.

Conflict of interest: The donation of public funds to a private non-profit organization also raises concerns regarding conflicts of interest if members of the board governing the governmental agency, which opts to transfer the funds, also serve on the board of directors of the private organization. Whether a conflict actually exists is a fact-based determination which does not lend itself to easy resolution, but consideration should be given to potential conflicts of interest in any transaction of this nature. As discussed in our 1988 opinion, the transfer of funds from a governmental agency to a private corporation could be void if the public duties of the board members who developed and approved the transfer proposal were in conflict with their interests in the private corporation. 1988 Iowa Op. Att'yGen. 112 (#88-10-2(L)) [1988 WL 247803], citing Wilson v. City of Iowa City, 165 N.W.2d 813, 820 (Iowa 1969). "By contrast, a government official who represents a governmental body on a separate 28E entity's governing board does not have an impermissible conflict of interest, at least absent litigation between the two entities." Id., citing Goreham v. Des Moines Metropolitan Area Solid Waste Agency, 179 N.W.2d 449, 462 (Iowa 1970).

Summary: Based upon examination of these authorities, I do not believe that a city library board may simply donate funds received from private donors to a private non-profit organization to use and invest as the nonprofit organization sees fit. Unless the library board retains the ability to oversee expenditures and to demand return of the funds in the event that future trustees do not agree with the delegation of control over the funds, the transaction violates the public purpose and non-delegation principles discussed above. Further, even if safeguards are put in place to assure ongoing oversight and control, I believe that the funds continue to be "public funds," subject to the deposit and investment standards contained in Code sections 12B and 12C and that the funds must be earmarked and spent for the purpose for which the gift was given.. A 28E agreement may provide a vehicle to facilitate joint public and private influence over the use of gifts received by a governmental body, by incorporating ongoing public oversight and accountability to the joint undertaking.

I am hopeful that this advice is useful to you in addressing issues related to the transfer of public funds. Please note, however, that this memorandum represents my own analysis of these sections and is not an opinion of the Attorney General. Feel free to contact me if you would like to discuss the issues further.