

The Top 5 Public Fund Investment Questions
Beth Grob
Ahlers & Cooney, P.C.

Public entities are often approached about investing public funds in various financial products that seem to earn a larger rate of return than what the market rate is at the time. Whether certain types of financial products are qualified investments under Iowa Code Chapter 12B may be an issue.

In general, in which type of investment products may public entities invest?

Iowa Code sections 12B.10(5)(a) and 12B.10(7) provide a very specific list of investment for public entities:

- (1) Obligations of the United States government, its agencies, and instrumentalities.
- (2) Certificates of deposit and other evidences of deposit at federally insured depository institutions approved pursuant to chapter 12C.
- (3) Prime bankers' acceptances that mature within two hundred seventy days and that are eligible for purchase by a federal reserve bank, provided that at the time of purchase no more than ten percent of the investment portfolio shall be in investments authorized by this subparagraph and that at the time of purchase no more than five percent of the investment portfolio shall be invested in the securities of a single issuer.
- (4) Commercial paper or other short-term corporate debt that matures within two hundred seventy days and that is rated within the two highest classifications, as established by at least one of the standard rating services approved by the superintendent of banking by rule adopted pursuant to chapter 17A, provided that at the time of purchase no more than five percent of all amounts invested in commercial paper and other short-term corporate debt shall be invested in paper and debt rated in the second highest classification, and provided further that at the time of purchase no more than ten percent of the investment portfolio shall be in investments authorized by this subparagraph and that at the time of purchase no more than five percent of the investment portfolio shall be invested in the securities of a single issuer.
- (5) Repurchase agreements whose underlying collateral consists of the investments set out in subparagraph (1) if the political subdivision takes delivery of the collateral either directly or through an authorized custodian. Repurchase agreements do not include reverse repurchase agreements.
- (6) An open-end management investment company registered with the federal securities and exchange commission under the federal Investment Company Act of 1940, 15 U.S.C. § 80(a), and operated in accordance with 17 C.F.R. § 270.2a-7.
- (7) A joint investment trust organized pursuant to chapter 28E prior to and existing in good standing on the effective date of this Act or a joint investment trust organized pursuant to chapter 28E after April 28, 1992, provided that the joint investment trust shall either be rated within the two highest classifications by at least one of the standard rating services approved by the superintendent of banking by rule adopted pursuant to chapter 17A and operated in accordance with 17 C.F.R. § 270.2a-7, or be registered with the federal securities and exchange commission under the federal Investment Company Act of 1940, 15 U.S.C. § 80(a), and operated in

accordance with 17 C.F.R. § 270.2a-7. The manager or investment advisor of the joint investment trust shall be registered with the federal securities and exchange commission under the Investment Advisor Act of 1940, 15 U.S.C. § 80(b).

(8) Notwithstanding sections 12C.2, 12C.4, 12C.6, 12C.6A, and any other provision of law relating to the deposits of public funds, if public funds are deposited in a depository, as defined in section 12C.1, any uninsured portion of the public funds invested through the depository may be invested in certificates of deposit arranged by the depository that are issued by one or more federally insured banks or savings associations regardless of location for the account of the public funds depositor if all of the following requirements are satisfied:

a. The full amount of the principal and any accrued interest of each certificate of deposit issued shall be covered by federal deposit insurance.

b. The depository, either directly or through an agent or subcustodian, shall act as custodian of the certificates of deposit.

c. The day the certificates of deposit are issued, the depository shall have received deposits in an amount eligible for federal deposit insurance from, and issued certificates of deposit to, customers of other financial institutions wherever located that are equal to or greater than the amount of public funds invested under this subsection by the public funds depositor through the depository.

Public entities may NOT invest in (1) reverse repurchase agreements; or (2) future and options contracts.

Can public entities invest in money market funds?

Yes, under certain circumstances. See number 6 above.

If so, what types of money market funds?

A public entity may only invest in a money market fund that is *registered with the federal securities and exchange commission under the federal Investment Company Act of 1940, 15 U.S.C. § 80(a), and operated in accordance with 17 C.F.R. § 270.2a-7* (see number 6 above).

How do you determine if a money market fund is registered with the S.E.C. and operated in accordance with S.E.C. rule 2a-7?

(1) Any money market fund registered with the S.E.C. will have a prospectus or information statement, a copy of which the municipality must receive. The prospectus/information statement *should plainly state* in the body of the document that it is registered with the S.E.C. and operated in accordance with S.E.C. rule 2a-7.

(2) If a money market fund is registered with the S.E.C. that money market fund is required to make certain quarterly and annual filings with the S.E.C. and which are available on the S.E.C.'s website at <http://www.sec.gov/edgar/searchedgar/webusers.htm>.

Is a verbal confirmation that the money market fund is an authorized investment sufficient?

No. It is incumbent on public entities to perform due diligence in determining on their own if an investment fits within the law. A verbal representation that an investment qualifies is not sufficient. A copy of the documents identified in the previous question MUST be requested and retained by the municipality.

In this record-low interest rate environment and the ever-increasing number of financial products available for investment, it may be wise for public entities to review its investment policies and practices and to consult with legal counsel.

The purpose of this article is to identify issues. It does not purport to be exhaustive or to render legal advice. You should consult with qualified counsel or other professionals in developing responses to specific situations.