

MEMORANDUM OF LAW

DATE: June 22, 1987

TO: Ed Ryan, Auditor and Comptroller, and Pat
Frazier, Director, Financial Management
FROM: City Attorney
SUBJECT: Capital Outlay Fund - Investment of - Use of
Interest Earned for Non-Capital Outlay Fund
Purposes

In view of the significant effect on the City's process of budgeting funds, you have asked that we give additional thought to the conclusion reached in the attached memorandum of law dated February 10, 1987. As you know, that memorandum of law concludes that interest earned on Capital Outlay Fund monies must be kept in the Capital Outlay Fund and used for Capital Outlay purposes. You have indicated that the current average amount in the City's Capital Outlay Fund is approximately \$70 million and that, based upon a prior opinion of this office, the interest earned on the Capital Outlay Fund has, for a number of years, been placed into the General Fund.

We have rereviewed the case and statutory law and must again conclude that interest earned on Capital Outlay Fund monies must be used for Capital Outlay Fund purposes.

A significant issue in determining whether the interest can or must be placed in the City's General Fund arises out of Section 53647(a) of the Government Code of the State of California which provides:

Interest; payment into fund

(a) Interest on all money deposited belongs to, and shall be paid quarterly into the general fund of, the local agency represented by the officer making the deposit, unless otherwise directed by law.

Section 53647 is part of Chapter 4, Division 2, Title 5 of the Code commencing with Section 53600, which chapter provides a

method for cities and counties to conduct their financial affairs. Section 53600 was amended, effective January 1, 1985, to include charter cities within the meaning of "local agency" governed by the terms of Chapter 4. Section 53630 was also amended at that time to include charter cities within the meaning of "local agency." Section 53630 through 53684 deals specifically with the deposit of funds by cities and counties.

The above quoted Section 53647 would appear to require the deposit of all interest earned on the various City funds to be

deposited into the General Fund. However, the provision does contain the key phrase "unless otherwise directed by law." There have been several court decisions dealing with the issue of whether or not interest earned on different types of funds should properly be deposited into the General Fund of counties or whether such interest should be distributed with principal to the designated recipient of the principal. In each reported case the courts have concluded that Section 53647 does not control and that, in effect, in the case of trust funds or funds in the nature of trust funds, the interest must follow the principal. The following are excerpts from West's Annotated California Government Code:

Mandamus was proper remedy to compel county treasurer to credit interest earned on funds deposited in law library fund to that fund where facts were stipulated. Board of Law Library Trustees of Los Angeles County v. Lowery, 154 P.2d 719, 67 Cal.App.2d 480 (1945).

Condemnees were entitled to interest actually earned on their share of funds paid into court pursuant to judgment. Redevelopment Agency of City and County of San Francisco v. Goodman, 125 Cal.Rptr. 818, 53 Cal.App. 3d 424 (1975).

The superior court is on a parity with other depositing "local agencies" within Depositary Act and hence superior court is in control of deposited funds and owner of any interest earned thereon which ownership is that of a trustee for person ultimately determined by the court to be entitled to receive the money from it, and such determination relates back to time of initial deposit of fund in court. Ostly v. Saper, 305 P.2d 946, 147 Cal.App.2d 671 (1957).

Where water district deposited with clerk moneys in order to secure immediate possession of lands sought to

be condemned and clerk turned over such deposits to county treasurer who commingled them with other funds and deposited all funds in various banks at interest, the Superior Court which held the entire sum, principal together with accretions of interest, as custodian for the water district was entitled to interest under Depositary Act, and where final judgments in condemnation proceedings had been satisfied, the Superior Court was required to return any balance of principal or interest to the water district.

Metropolitan Water Dist. of Southern Cal. v. Adams, 197

P.2d 543, 32 Cal.2d 620 (1948).

School district maintaining funds in county treasury was entitled to interest earned on school funds commingled and deposited in bank with county funds by county treasurer in absence of statute that county should be entitled to all interest earned on such commingled funds deposited by treasurer. Pomona City School Dist. v. Payne, 50 P.2d 822, 9 Cal.App.2d 510 (1935).

Interest earned on monies deposited in civil actions is to be returned to owner of monies, rather than retained by county as part of its general fund. Fresno Fire Fighters Local 753 v. Jernagan, 222 Cal. Rptr. 886, 177 Cal.App.3d 403 (App.5 Dist.1986).

In addition, please see the attached California Attorney General's opinion dated January 8, 1976, which involves a fact situation similar in many ways to our own, and which concluded that school districts may not transfer interest earned on earthquake safety funds from the earthquake safety fund to the general fund.

Also, as you know, the California Teachers' Association recently obtained a superior court judgment that the interest earned on the State lottery education fund is not subject to the provisions of Government Code Section 53647 but is in the nature of a trust fund where interest earned must follow the principal. A copy of the Points and Authorities on both sides of that case is also attached for your information.

In view of all of the above cases, together with the attached Attorney General's opinion, we must again opine that our memorandum of law dated February 10, 1987, (attached) is correct in its conclusion that interest earned on Capital Outlay funds must remain in the Capital Outlay Fund and must be used for Capital Outlay purposes.

It is our understanding that your past pattern of depositing such interest into the General Fund, based upon an earlier memorandum from this office, has not resulted in any significant detriment to the Capital Outlay Fund since a practice has been followed by the City of depositing substantial sales tax revenues into the Capital Outlay Fund even though such sales tax revenues could have been deposited into the City's General Fund. We understand that the amounts of such deposits, as well as other amounts the City may have voluntarily deposited into the Capital Outlay Fund have, in effect, offset the interest revenues which have been removed from the Capital Outlay Fund.

Based upon such understanding, it is our conclusion that it

is not necessary to reimburse the Capital Outlay Fund for past interest earned. It may be appropriate, after you have had an opportunity to review this memorandum, to schedule a meeting to discuss other City funds which may constitute trust funds and be subject to the same rules as are applicable to the Capital Outlay Fund.

JOHN W. WITT, City Attorney

By

Harold O. Valderhaug

Deputy City Attorney

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Attachments 3

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