October 27, 1993

OPINION NO. 93-021

The Honorable Thomas E. Ferguson
Auditor of State
P.O. Box 1140
Columbus, Ohio 43266-0040

Dear Auditor Ferguson:

You have requested an opinion regarding the permissibility of investments by subdivisions in mortgaged-backed securities which are issued or guaranteed by the Federal National Mortgage Association ("FNMA"). Specifically, you have posed three questions, which may be paraphrased as follows:

1. Does R.C. 135.14 authorize a treasurer or governing board to invest in instruments that do not mature within two years from the date of purchase, but that can be sold within two years from the date of purchase?

2. Does R.C. 135.14(B) authorize a treasurer or governing board to invest in instruments issued by FNMA?

3. If a treasurer or governing board is not authorized, pursuant to R.C. 135.14(B), to invest in instruments issued by FNMA, does federal law supplant or preempt state law to allow such investments?

I. Investment of Moneys by Subdivisions

R.C. 135.01-.21 sets forth provisions concerning the investment of moneys by subdivisions.[1]

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[1] Except as otherwise provided in R.C. 135.14 and R.C. 135.18, the term "subdivision," for purposes of R.C. 135.01-.21, means

> any municipal corporation, except one which has adopted a charter under Article XVIII, Ohio Constitution, and the charter or ordinances of the chartered municipal corporation set forth special provisions respecting the deposit or investment of its public moneys, or any school district including a county school district, a county school financing district, township, municipal or school district sinking fund, special taxing or assessment district, or other district or local authority electing or appointing a treasurer, except a county. In the case of a school district, special taxing or assessment district, or other local authority for which a treasurer, elected or appointed primarily as the treasurer of

R.C. 135.14, which authorizes the investment of interim moneys by subdivisions, provides, in part:

> The treasurer or governing board may invest or deposit any part or all of the interim moneys, *provided that such investments will mature or are redeemable within two years from the date of purchase,* except as otherwise limited in this section. The following classifications of obligations shall be eligible for such investment or deposit:
> (A) Bonds, notes, or other obligations of or guaranteed by the United States, or those for which the faith of the United States is pledged for the payment of principal and interest thereon;
> (B) Bonds, notes, debentures, or other obligations or securities issued by any federal government agency, or the export-import bank of Washington;
> (C) Interim deposits in the eligible institutions applying for interim moneys as provided in section 135.08 of the Revised Code....
> (D) Bonds and other obligations of this state;
> (E) No-load money market mutual funds consisting exclusively of obligations described in division (A) or (B) of this section and repurchase agreements secured by such obligations, provided that investments in securities described in this division are made only through eligible institutions mentioned in section 135.03 of the Revised Code.
> The treasurer or governing board may also enter into a written repurchase agreement that sets forth the terms and conditions of the agreement between the parties for a period not to exceed thirty days with any eligible institution mentioned in section 135.03 of the Revised Code, under the terms of which agreement the treasurer or governing board purchases, and such institution agrees unconditionally to repurchase any of the securities listed in division (A) or (B) of this section that will mature or are redeemable within five years from the date of purchase. (Emphasis added.)

R.C. 135.14 thus authorizes a subdivision's treasurer or governing board to invest or deposit the subdivision's interim moneys in specific statutorily enumerated instruments that either will mature or are redeemable within two years from the date of purchase.

II.A Subdivision May Not Invest in Those Instruments Listed in R.C. 135.14 that Do Not Mature Within Two Years but that Can Be Sold in the Market at the Option of the Treasurer or Governing Board within Two Years from the Date of

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> a subdivision, is authorized or required by law to act as ex officio treasurer, the subdivision for which such a treasurer has been primarily elected or appointed shall be considered to be the "subdivision." The term also includes a union or joint institution or enterprise of two or more subdivisions, that is not authorized to elect or appoint a treasurer, and for which no ex officio treasurer is provided by law.

R.C. 135.01(L).

Purchase

In your first question you are concerned with the authority of a subdivision's treasurer or governing board to invest in instruments that do not mature within two years from the date of purchase, but that can be sold within two years from the date of purchase. As noted above, a subdivision's treasurer or governing board is specifically empowered to invest the subdivision's interim moneys in those instruments listed in R.C. 135.14 that are redeemable within two years from the date of purchase.

While there is no applicable definition of "redeemable" in the Ohio Revised Code, in ordinary usage, "redeemable" means "[s]ubject to redemption; admitting of redemption or repurchase; given or held under conditions admitting of reacquisition by purchase." *Black's Law Dictionary* 1278 (6th ed. 1990). *See generally* R.C. 1.42 ("[w]ords and phrases shall be read in context and construed according to the rules of grammar and common usage"). "Redemption" is

> The reacquisition of a security by the issuer pursuant to a provision in the security that specifies the terms on which the reacquisition may take place. A security is called for redemption when the issuer notifies the holder that the redemption privilege has been exercised....
> A repurchase; a buying back....
> ....
> Repurchase of notes, bonds, stock, bills, or other evidences of debt, by paying their value to their holders. The payment of principal and unpaid interest on bonds or other debt obligations.
> Repurchase by corporation of its shares at a price equal to the net asset value of the shares on date a redemption request is received by the corporation.

Black's Law Dictionary at 1278. The General Assembly's use of the term "redeemable" in R.C. 135.14, accordingly, evidences a legislative intent to authorize a subdivision's treasurer or governing board to invest the subdivision's interim moneys in those instruments listed in R.C. 135.14 that are subject to repurchase by the issuer within two years from the date of purchase. *See generally* 15 U.S.C. §80a-2(a) (1988) (as used in Title 15, "unless the context otherwise requires-.... (32) "Redeemable security" means any security, other than short-term paper, under the terms of which the holder, upon its presentation to the issuer or to a person designated by the issuer, is entitled (whether absolutely or only out of surplus) to receive approximately his proportionate share of the issuer's current net assets, or the cash equivalent thereof").

In light of the above, it is clear that the fact that an instrument can be converted into cash by sale in the market at the option of the treasurer or governing board of a subdivision within two years from the date of purchase does not qualify such instrument as an investment that is redeemable within two years from the date of purchase. Accordingly, R.C. 135.14 does not authorize a treasurer or governing board of a subdivision to invest the subdivision's interim moneys in those instruments listed in R.C. 135.14 that do not mature and are not redeemable within two years of the date of purchase, even though they may be convertible into cash by sale in the market at the option of the treasurer or

governing board within two years from the date of purchase.

III.A Subdivision May Not Invest in Instruments Issued by FNMA

Your second question asks whether R.C. 135.14(B) authorizes a subdivision's treasurer or governing board to invest in instruments issued by FNMA. Division (B) of R.C. 135.14 authorizes a treasurer or governing board to invest in "[b]onds, notes, debentures, or other obligations or securities issued by any federal government agency, or the export-import bank of Washington" that will mature or are redeemable within two years from the date of purchase. Accordingly, if FNMA is a federal government agency, a subdivision's treasurer or governing board is authorized to invest in instruments issued by FNMA that will mature or are redeemable within two years from the date of purchase.

A.The Creation of FNMA

In the National Housing Act, ch. 847, 48 Stat. 1246 (1934), Congress authorized the creation of private national mortgage associations to engage in secondary market activity. Although the Act did not contain any explicit authorization for the creation of a federal mortgage association, section four of the National Housing Act Amendments of 1938, ch. 13, 52 Stat. 8, 23 did contain language which provided implicit authorization for the creation of FNMA as a subsidiary of the Reconstruction Finance Corporation ("RFC"). *See* Bartke, *Fannie Mae and the Secondary Mortgage Market,* 66 Nw. U.L. Rev. 1, 18 (1971).

In the Housing Act of 1948, ch. 784, 62 Stat. 1206, Congress repealed the authorization for the chartering of private national mortgage associations and provided the FNMA its first explicit statutory authorization. In 1950, FNMA was moved from the RFC to the Housing and Home Finance Agency ("HHFA"). Reorganization Plan No. 22 of 1950, 64 Stat. 1277. FNMA "remained a constituent agency of HHFA, and later of the Department of Housing and Urban Development [("HUD")], until the passage of Title VIII in 1968." Bartke, *Fannie Mae and the Secondary Mortgage Market,* 66 Nw. U.L. Rev. at 21.

As FNMA became more and more a means of maintaining low interest rates on certain types of mortgages, the fact that its activities were capitalized through borrowing from the federal treasury created the need for successive and greater borrowing authorizations. *Id.* FNMA, thus, was a substantial drain on the federal treasury. *Id.*

To alleviate this drain on the federal treasury, FNMA was rechartered as a federal corporation and its functions were divided into (1) the special assistance functions, (2) the management and liquidating functions, and (3) the secondary market operations. Housing Act of 1954, ch. 649, §§304-306, 68 Stat. 590, 615-19. Since the secondary market operation was depleting the federal treasury and it was believed that this function could be self-supporting and privately capitalized, *see* Bartke, *Fannie Mae and the Secondary Mortgage Market,* 66 Nw. U.L. Rev. at 21-24, the financing of this function was transferred from the public sector to the private sector, while the special assistance functions and the management and liquidation functions continued to be financed through borrowing from the federal treasury.

In 1968 the original FNMA was divided into two separate and distinct corporations, the new FNMA, which is a government-sponsored private corporation, and the newly created Government National Mortgage Association ("GNMA"), which is specifically made part of HUD. Housing and Urban Development Act of 1968, Pub. L. No. 90-448, Title VIII, §801, 82 Stat. 476, 536 (codified at 12 U.S.C. §1716b (1988)). GNMA retained control over the special assistance functions and the management and liquidating functions, *see* 12 U.S.C. §1717(a)(2)(A) (1988), while the secondary mortgage activity was completely turned over to the new FNMA, *see* 12 U.S.C. §1717(a)(2)(B) (1988). Housing and Urban Development Act of 1968, Pub. L. No. 90-448, Title VIII, §801, 82 Stat. 476, 536.

B.The Financing and Management of FNMA

Because the original FNMA's secondary market operation had proven economically sound and capable of being financed solely from private sources, Congress specifically made the new FNMA a privately owned and privately financed corporation. Housing and Urban Development Act of 1968, Pub. L. No. 90-448, U.S. Code Cong. & Admin. News (82 Stat. 476) 2877, 2943-44. Pursuant to 12 U.S.C. §1718 (1988 & Supp. IV 1992), the new FNMA maintains the capital structure of a privately owned corporation. The ownership of the new FNMA thus has been turned over to private shareholders.

In addition, the federal government's control over the management of the new FNMA is limited. FNMA's board of directors consists of five persons appointed by the President of the United States and thirteen persons elected by the common stockholders. 12 U.S.C. §1723(b) (1988 & Supp. IV 1992). "Within the limitations of law and regulation, the board shall determine the general policies which shall govern the operations of the [FNMA], and shall have power to adopt, amend, and repeal bylaws governing the performance of the powers and duties granted to or imposed upon it by law." *Id.* The board of directors thus is statutorily authorized to manage the corporation. In contrast, the federal government's control over the management of the new FNMA is limited to the exercise of general regulatory power over the FNMA, *see* 12 U.S.C. §1719(b)-(e) (1988 & Supp. IV 1992), and approving the capital distributions from general surplus accounts, 12 U.S.C. §1718(c) (1988 & Supp. IV 1992).

C.FNMA Is Not a Federal Government Agency

An examination of the history, financing, and management of FNMA ineluctably leads to one conclusion: The FNMA is not a federal government agency. The fact that 12 U.S.C. §1716b (1988) provides that FNMA is a "Government-sponsored private corporation," *see also* 12 U.S.C. §1717(a)(2)(B) (1988), while GNMA remains a part of HUD, 12 U.S.C. §1717(a)(2)(A) (1988), *see also* 12 U.S.C. §1716b (1988) evidences an emphatic congressional intent that FNMA is no longer a governmental agency, but is a private agency. S*ee In re Werts,* 36 Bankr. 799, 801-02 (E.D. Pa. 1984), *rev'd on other grounds,* 48 Bankr. 980 (E.D. Pa. 1985); *see also* 12 U.S.C. §1719(d) (1988 & Supp. IV 1992) (FNMA shall insert appropriate language in all of the securities issued under 12 U.S.C. §1719 "clearly indicating that such securities, together with the interest thereon, are not guaranteed by the

United States and do not constitute a debt or obligation of the United States or any agency or instrumentality thereof other than the corporation"). FNMA also is financed and operated by private shareholders. Moreover, the federal government's control over management is limited to the exercise of general regulatory power over FNMA. In light of the foregoing, it must be concluded that FNMA is not a federal government agency; thus, the treasurer or governing board of a subdivision is not authorized, pursuant to R.C. 135.14(B), to invest the subdivision's interim moneys in instruments issued by FNMA.

IV. Subchapter 12 U.S.C. §§1716-1723i (1988 & Supp. IV 1992) Does Not Preempt R.C. 135.14

Your final question asks whether, if a treasurer or governing board is not authorized, pursuant to R.C. 135.14(B), to invest in instruments issued by FNMA, does federal law preempt state law to allow such investments. "Federal law preempts state regulation when Congress intends to displace state law." *Ash v. Board of Review,* 26 Ohio St. 3d 158, 162, 497 N.E.2d 724, 727 (1986); *accord Mowery v. Mercury Marine, Div. of Brunswick Corp.,* 773 F. Supp. 1012 (N.D. Ohio 1991); *Kemp v. Raudabaugh,* 76 Ohio App. 3d 488, 491-92, 602 N.E.2d 389, 391 (Auglaize County 1991); *see also In re White Motor Credit Corp.,* 75 Bankr. 944, 950 (N.D. Ohio 1987) ("[f]ederal pre-emption of state law must be explicit or compelled due to an unavoidable conflict between the federal and state law").

No provision in subchapter 12 U.S.C. §§1716-1723i (1988 & Supp. IV 1992) (which provides for the creation and operation of FNMA) expressly requires or authorizes the subdivisions of the various states to invest in instruments issued by FNMA. In addition, there is no explicit or implicit preemption evident from a review of subchapter 12 U.S.C. §§1716-1723i (1988 & Supp. IV 1992). Congress thus has not determined that the subdivisions of the various states must be authorized to invest in instruments issued by FNMA. In the absence of a congressional intention to the contrary, it must be concluded that R.C. 135.14 is not preempted by subchapter 12 U.S.C. §§1716-1723i (1988 & Supp. IV 1992).

V. Conclusions

Based on the foregoing, it is my opinion, and you are hereby advised, that:

1. R.C. 135.14 does not authorize the treasurer or governing board of a "subdivision," as defined in R.C. 135.01(L), to invest the subdivision's interim moneys in those instruments listed in R.C. 135.14 that do not mature and are not redeemable within two years of the date of purchase, even though they may be convertible into cash by sale in the market at the option of the treasurer or governing board within two years from the date of purchase.

2. The treasurer or governing board of a "subdivision," as defined in R.C. 135.01(L), is not authorized to invest the subdivision's interim moneys in instruments issued by the Federal National Mortgage Association.

3.Subchapter 12 U.S.C. §§1716-1723i (1988 & Supp. IV 1992) does not preempt R.C. 135.14 so as to allow the treasurer or governing board of a "subdivision," as defined in R.C. 135.01(L), to invest the subdivision's interim moneys in instruments issued by the Federal National Mortgage Association.

Respectfully,

LEE FISHER
Attorney General

October 27, 1993

The Honorable Thomas E. Ferguson
Auditor of State
P.O. Box 1140
Columbus, Ohio 43266-0040

SYLLABUS: 93-021

1. R.C. 135.14 does not authorize the treasurer or governing board of a "subdivision," as defined in R.C. 135.01(L), to invest the subdivision's interim moneys in those instruments listed in R.C. 135.14 that do not mature and are not redeemable within two years of the date of purchase, even though they may be convertible into cash by sale in the market at the option of the treasurer or governing board within two years from the date of purchase.

2. The treasurer or governing board of a "subdivision," as defined in R.C. 135.01(L), is not authorized to invest the subdivision's interim moneys in instruments issued by the Federal National Mortgage Association.

3. Subchapter 12 U.S.C. §§1716-1723i (1988 & Supp. IV 1992) does not preempt R.C. 135.14 so as to allow the treasurer or governing board of a "subdivision," as defined in R.C. 135.01(L), to invest the subdivision's interim moneys in instruments issued by the Federal National Mortgage Association.