VOLUME NO. 44 **OPINION NO. 5**

CITIES AND TOWNS - Authority of self-governing city to establish capital improvement fund;
LOCAL GOVERNMENT - Authority of self-governing city to establish capital improvement fund;
MUNICIPAL CORPORATIONS - Authority of self-governing city to establish capital improvement fund;
PUBLIC FUNDS - Authority of self-governing city to establish capital improvement fund;
MONTANA CODE ANNOTATED - Sections 2-7-501 to 2-7-521, 7-1-101, 7-1-113, 7-1-114, 7-6-4134, 7-6-4231, 7-13-4307, 7-13-4325;
MONTANA CONSTITUTION - Article VIII, section 11; Article XI, section 6;
OPINIONS OF THE ATTORNEY GENERAL - 43 Op. Att'y Gen. No. 53 (1990), 43 Op. Att'y Gen. No. 41 (1989), 42 Op. Att'y Gen. No. 120 (1988), 38 Op. Att'y Gen. No. 14 (1979), 37 Op. Att'y Gen. No. 68 (1977).

HELD: 1. The equipment reserve account in an internal service fund established by a city with self-government powers is a "capital improvement program fund" within the meaning of section 7-6-4134, MCA.

2. Under section 7-6-4134, MCA, a self-governing city may not retroactively transfer from the general fund an amount exceeding 5 percent of the money received from the all-purpose levy.

3. Equipment reserve accounts in enterprise funds must be maintained separately from other equipment reserve accounts in a capital improvement fund.

4. Section 7-6-4134, MCA, does not prohibit the transfer of funds to an equipment reserve account from sources other than the all-purpose levy fund.

February 11, 1991

Charles Brooke, Director
Department of Commerce
1424 Ninth Avenue
Helena MT 59620

Dear Mr. Brooke:

You have requested my opinion on several questions concerning a self-governing city's equipment reserve account. In particular, you ask:

1. Is an equipment reserve account within an internal service fund established by a self-governing city a "capital improvement program fund" as defined in section 7-6-4134, MCA?

2. If so, may the city make a one-time retroactive transfer of money from its all-purpose levy revenues to the internal service fund in excess of the 5 percent limitation in section 7-6-4134, MCA?

3. May the city also transfer to the equipment reserve account from "enterprise funds" revenues generated from income-producing municipal services in order to replace equipment used in providing those services?

4. May the city transfer to the equipment reserve account funds from sources other than the all-purpose levy fund

> and enterprise funds in order to help replace equipment used in providing the services?

This matter arises from an audit of a self-governing city for the fiscal year ending June 30, 1989. One of the reasons for the audit was the large amount of cash reserves in the city's "internal service funds." These funds, called the "central garage internal service fund" and the "data processing internal service fund," are used for providing and maintaining adequate equipment for city departments. Prior to 1989, the main source of revenue for these funds was fees charged to other city departments for reimbursement of the support services. However, in fiscal year 1989 there was a substantial increase in the balance of the central garage fund. The balance of the fund at the end of fiscal year 1988 was $247,123, and the balance at the end of fiscal year 1989 was $4,454,369.

Pursuant to its authority in sections 2-7-501 to -521, MCA, the Department of Commerce (department) requested a supplemental report from the auditors who did the 1988-89 audit. The auditors were asked to trace the source of the $3 million increase in the central garage fund. I am assuming that the following figures from the audit are accurate: $1,363,534 came from the general fund supported by all-purpose levy revenues; $1,002,069 came from certain "special revenue funds," including the special funds established for planning, federal block grants, street maintenance district, and boulevard maintenance district; and $656,895 came from "enterprise funds" which include funds established through provision of income-producing services, including water and sewer services, the city's multi-sport complex, and city parking. The transferred funds were used to establish an "equipment reserve account" within the central garage internal service fund to provide for future equipment replacement.

These transfers caused concern in light of section 7-6-4134, MCA, which provides:

> **Capital improvement program fund.** An amount not to exceed 5% of the money received from and as a part of the aforesaid all-purpose levy may be placed in a separate fund, known as the capital improvement program fund, to be earmarked for the replacement and acquisition of property, plant, or equipment costing in excess of $5,000, with a life expectancy of 5 years or more, provided that a capital improvement program has been formally adopted by city or town ordinance.

The city had levied 95.07 mills for its all-purpose levy for fiscal year 1989, each mill having a value of $53,612. The total all-purpose levy for fiscal year 1989 was therefore $5,096,893. The city transferred from the general fund a lump sum of $1,363,534. While it is unclear from the materials you gave

me how much of the general fund transfer came from all-purpose levy revenues, I am assuming for the purposes of this opinion that all of the $1,363,534 came from the levy revenues. With this assumption, nearly 30 percent of the revenues received from the all-purpose levy were transferred into the internal service funds.

Your first question is whether the internal service funds are capital improvement funds and therefore regulated by section 7-6-4134, MCA. My analysis is based on the assumption that the city transferred the funds in accordance with section 7-6-4123, MCA, which provides: "No money must be transferred from one fund to another except by ordinance or resolution of the council." If the council has failed to comply with this section, clearly the transfers were inappropriate from their inception.

The audit report concluded that the central garage fund meets the description of a capital improvement fund in section 7-6-4134, MCA. The fund includes specifically an "equipment reserve account" created expressly for the replacement and acquisition of property, plant, and equipment as described in section 7-6-4134, MCA. I must therefore concur with the report that the equipment reserve account of the central garage fund meets the description of a capital improvement fund in section 7-6-4134, MCA.

The answer to your next question requires examination of whether the city is subject to the provisions of section 7-6-4134, MCA. The city in question has adopted a self-government charter. "A local government unit adopting a self-government charter may exercise any power not prohibited by this constitution, law, or charter." Mont. Const. Art. XI, § 6; § 7-1-101, MCA. As a self-governing local government unit, the city has the authority to "share powers with the state government." D & F Sanitation Service v. City of Billings, 219 Mont. 437, 713 P.2d 977, 981-82 (1986). While the shared powers concept does not leave the local government unit free from state control, the concept embodies the "'assumption that local government *possesses* the power, unless it has been specifically denied.'" D & F Sanitation, 713 P.2d at 982 (quoting II Mont. Const. Conv. 796-97 (1972)) (emphasis in original); 43 Op. Att'y Gen. No. 41 (1989), 43 Op. Att'y Gen. No. 53 (1990). To determine whether a self-governing city has certain powers, it is necessary to:

> 1) consult the charter and consider constitutional ramifications; 2) determine whether the exercise is prohibited under the various provisions of [Title 7, chapter 1, part 1, MCA] or other statute specifically applicable to self-government units; and 3) decide whether it is inconsistent with state provisions in an area affirmatively subjected to state control as defined by section [7-1-113].

37 Op. Att'y Gen. No. 68 at 272, 274 (1977), 43 Op. Att'y Gen. No. 41 (1989), 43 Op. Att'y Gen. No. 53 (1990).

There is nothing in the city's charter addressing the transfer of city funds. However, two constitutional provisions broadly address the city's responsibility with respect to accountability and use of funds. "All money borrowed by or on behalf of the state or any county, city, town, or other local governmental entity shall be used only for purposes specified in the authorizing law." Mont. Const. Art. VIII, § 11. Further, Article VIII, section 12 requires the Legislature to "insure strict accountability of all revenue received and money spent by the state and counties, cities, towns, and all other local governmental entities." These constitutional provisions necessarily impose accountability limitations on transfer of city monies from one fund to another.

With respect to the statutory limitations on the powers of self-governing units, the second step of the analysis quoted above requires consideration of sections 7-1-111 and 7-1-112, MCA, which limit the exercise of power of self-governing units, and section 7-1-114, MCA, which lists the mandatory provisions with which a self-governing unit must comply. Neither section 7-1-111 nor section 7-1-112, MCA, addresses budgetary matters. However, section 7-1-114(g), MCA, expressly provides that a local government with self-governing powers is subject to

> [a]ny law regulating the budget, finance, or borrowing procedures and powers of local governments, except that the mill levy limits established by state law shall not apply[.]

Further, section 7-1-114(2), MCA, requires that "[t]hese provisions are a prohibition on the self-government unit acting other than as provided." Section 7-6-4134, MCA, by its clear terms, is a law regulating the budget procedures of a city. As such, the 5 percent limitation in section 7-6-4134, MCA, is a mandatory provision with which a city must comply in establishing its budget.

The city suggests that the decision of State ex rel. Swart v. Molitor, 190 Mont. 515, 621 P.2d 1100 (1981), may dictate an opposite conclusion. I do not believe that Molitor controls your questions concerning the all-purpose levy revenues. In Molitor, the court concluded that the mandatory provision requiring compliance with state laws regulating planning and zoning did not apply to the fees charged by a county surveyor in examining certificates of survey. The court reasoned that a particular statutory section allowed for such review and that the remaining sections were silent with respect to prescribing a fee. 621 P.2d at 1103-04. Relying upon the shared powers concept, and because there was no statute forbidding self-government units from assessing a fee, the Court held that the fee was valid.

Here, the state statutes are not silent with respect to all-purpose levy revenues and the establishment of capital improvement funds. Section 7-6-4134, MCA, gives express direction in this area. The city, despite its status as a self-governing city, is therefore subject to section 7-6-4134, MCA, and other similar laws setting budgetary procedures. See also Billings Firefighters Local 521 v. City of Billings, 214 Mont. 481, 694 P.2d 1335 (1985) (under section 7-1-114(f), MCA, a self-governing city may not supersede statutes requiring that a city maintain a municipal fire department).

You also ask whether a retroactive transfer of more than 5 percent of the all-purpose levy revenues for fiscal year 1989 is compatible with the provisions of section 7-6-4134, MCA. The audit suggests that more than 5 percent of the all-purpose levy revenues may be transferred in fiscal year 1989 because there have not been any such transfers previously. The audit then concludes that a retroactive transfer would be allowable because the lump sum may be retroactively applied as transfers from the past six years. I cannot accept the audit's interpretation of section 7-5-4134, MCA. If such retroactive transfers were allowable, the 5 percent limitation in section 7-6-4134, MCA, would be rendered meaningless. A city could go back any number of years rationalizing the transfer of any amount to the equipment reserve account. The plain language of section 7-6-4134, MCA, prohibits a one-time retroactive transfer of funds exceeding the 5 percent limitation.

Your third question is whether equipment reserve accounts in "enterprise funds" may be transferred to the equipment reserve account in the central garage internal service fund. As you describe them, "enterprise funds" are funds generated from the provision of income-producing municipal services, such as water and sewer systems. Under section 7-13-4307, MCA, a city is authorized to accumulate such "reserves" as are necessary for the depreciation and replacement of utility services systems. However, section 7-13-4325, MCA, defines the accounting procedures for the water and sewer enterprise funds:

> After any municipality has issued and sold revenue bonds under this part, it must keep all income and revenues derived from the operation of the system separate and distinct from all other revenues and shall keep books and accounts for such system separate and distinct from all other books and accounts.

This section expressly prohibits the consolidation of revenues in the enterprise funds with revenues from other sources. Under section 7-1-114(1)(g), MCA, and the above reasoning with respect to application of section 7-6-4134, MCA, the city may not "reclassify" equipment reserves maintained in the enterprise funds. As such, equipment reserve accounts for enterprise funds must be maintained separately from such accounts in the capital improvement fund.

Nonetheless, section 7-13-4325, MCA, does not preclude the payment of monies to the central garage fund for the proportional use of the equipment maintained by the garage fund. Section 7-13-4328, MCA, provides that the amount of money pledged for payment of bonds does not include the "normal, reasonable, and current expenses of operation and maintenance." Therefore, the renting or leasing of equipment administered by an internal service fund would be allowable as a necessary and reasonable expense. In Greener v. City of Great Falls, 157 Mont. 376, 485 P.2d 932 (1971), the Supreme Court upheld the use of special funds for the construction of shop and storage buildings used to house city vehicles and equipment. The amount paid from each special fund depended upon each fund's fair proportional share of vehicle maintenance cost. The Montana Supreme Court upheld the use of special funds for the construction project and stated:

> Each department clearly could expend its separate funds for maintenance and repair of its vehicles at a downtown garage operated by a private individual. It is equally clear that each department could commit its funds to construction of a separate repair facility for its own exclusive use, staffed by its own mechanic, and operated by its own personnel. In view of these considerations, we perceive no reason why each separate department cannot contribute these same funds to construction and operation of a joint use central repair facility in proportion to its anticipated use thereof. Nor do we see any reason why the source of the separate funds of the respective departments, unless otherwise obligated or prohibited, forecloses such contribution. The appropriation of a portion of such funds for construction costs of such joint use facility rests on the same authority that permits use of such funds to construct a separate repair facility for the exclusive use of each department.

485 P.2d at 942. While it is clear from the Greener decision that special funds may be used to purchase equipment or to construct buildings that would be used in providing the municipal services, the Greener decision does not sanction the transfer of the funds into a separate account for purposes that are not necessarily related to the proportionate use of equipment by the fund. Here, I have no facts as to what proportions would properly be allocated to which funds and therefore decline to determine whether the transfers could be considered a proper payment for proportional use of the equipment.

Your last question is whether section 7-6-4134, MCA, is a limitation on the transfer of funds from sources other than the all-purpose levy or enterprise funds. Section 7-6-4134, MCA, by its terms, places limits only on the revenues from the all-purpose levy and imposes no restrictions with respect to funds from other sources. You have not suggested that there is a state

statute or administrative rule that would prohibit such transfers from other sources.

Unlike the transfers from the all-purpose levy revenues and the enterprise funds, the law is silent with respect to special revenue funds. As a general rule,

> it is within the discretion of the legislative body of a city to segregate and divide moneys belonging to the municipality into whatever separate funds its convenience or caprice may dictate for administrative purposes, as long as it does not do so contrary to statute or its charter.

McQuillin, 15 Municipal Corporations § 39.44, at 159. This general principle is, of course, limited by the constitutional provision which requires that borrowed money may only be used for purposes specified in the authorizing law. Mont. Const. Art. VIII, § 11. This constitutional provision reflects the general prohibition that special funds may not be used for another and different purpose. McQuillin, 15 Municipal Corporations § 39.50, at 191.

Section 7-1-114(g), MCA, does not apply because there is no state budgetary law addressing such transfers. If the statutes are silent and the exercise of power is not expressly prohibited, then it makes no difference that the activity in question may fall within those subject areas addressed by the mandatory provisions of section 7-1-114, MCA. Molitor, *supra*, 621 P.2d at 1104. Thus, as long as state statutes or rules are silent in this area, I must conclude that there is not a conflict with state laws and that such transfers are not prohibited. See also Diefenderfer v. City of Billings, 223 Mont. 487, 726 P.2d 1362 (1986), reaffirming Molitor and recognizing the valid exercise of self-government powers when state law is silent.

You cite several previously issued Attorney General's Opinions suggesting that a self-governing city has no more authority than a city with general powers with respect to an area covered by section 7-1-114, MCA. In 38 Op. Att'y Gen. No. 14 at 51 (1979), it was recognized that local governments, whether vested with general or self-government powers, are bound by the state bonding procedures because bonding procedures come within the purview of section 7-1-114, MCA. This opinion was later characterized as stating, "Thus, with respect to the issuance of revenue bonds, local governments with self-government powers have no more powers than local governments with general government powers." 42 Op. Att'y Gen. No. 120 at 474 (1988). You rely upon this statement and subsection (2) of section 7-1-114, MCA, which prohibits a self-governing city from acting "other than as provided," to reach the conclusion that a self-governing city may not exercise any independent authority under areas covered by section 7-1-114, MCA. You suggest that a self-governing city may act *only* as provided by the statutes and, if statutes are

silent with respect to certain actions in the mandatory areas, the silence nevertheless prevents a self-governing city from taking any action. In light of Molitor and the statutory mandate requiring that local government powers be liberally construed, I cannot agree with your suggestions. See § 7-1-106, MCA. If a statute falls within the mandatory subjects in section 7-1-114, MCA, clearly a self-governing city must comply with the statute. Here, there is no statute expressly regulating or prohibiting the transfers of funds other than all-purpose levy funds or enterprise funds.

THEREFORE, IT IS MY OPINION:

1. The equipment reserve account in an internal service fund established by a city with self-government powers is a "capital improvement program fund" within the meaning of section 7-6-4134, MCA.

2. Under section 7-6-4134, MCA, a self-governing city may not retroactively transfer from the general fund an amount exceeding 5 percent of the money received from the all-purpose levy.

3. Equipment reserve accounts in enterprise funds must be maintained separately from other equipment reserve accounts in a capital improvement fund.

4. Section 7-6-4134, MCA, does not prohibit the transfer of funds to an equipment reserve account from sources other than the all-purpose levy fund.

Sincerely,

MARC RACICOT
Attorney General