DO THE CONSTITUTION AND STATUTES OF COLORADO
ALLOW THE STATE AND LOCAL GOVERNMENTS
TO ESTABLISH AND OPERATE PUBLIC BANKS?

LEGAL MEMORANDUM*

July 25, 2019

For purposes of this memorandum we shall define a public bank as a bank owned and operated by government. A few years ago, the Colorado Legislative Council and Office of Legislative Legal Services ("LC-OLLS"), in their Review and Comments memoranda in response to several successive ballot initiatives proposing a state-owned public bank, raised reasonable questions as to whether the Colorado constitution or statutes prohibit the establishment of public banks. The Review and Comment memos were prepared in compliance with Colorado statute C.R.S. 1-40-105(1). Consistent with the statutory duties of LC-OLLS, their memos did not include any legal memoranda, legal opinions, or legal research on the points they raise, but they did cite specific sections of the Constitution and statutes whose language would or might appear to raise questions as to the legality of public banks.

This memorandum provides legal research on each of the issues raised by LC-OLLS as well as a few other relevant legal issues, with a goal of determining whether the Colorado constitution and statutes currently allow the establishment of public banks. We encourage a thorough evaluation of our research to accurately assess the present state of Colorado law on each of these issues.

The correct answers to these questions will enable us to determine whether any constitutional amendments or statutory revisions are necessary or would be helpful to facilitate the establishment of successful public banks in Colorado.

Conclusion: In our opinion the Colorado constitution does not prohibit the state or any political subdivision from having its own public bank or banks. As we will show, the purpose of the constitutional provisions in question was to deal with problems quite different from public banks and how they are operated. Further, we conclude that a reasonable argument can be made that home rule cities and towns already have the right to establish their own public banks, and that the legislature could authorize home rule counties to establish their own public banks. However, we believe state legislation would be useful to clearly authorize home rule cities, towns, and counties to establish their own public banks, and to allow the state and local governments to obtain a state bank charter under state law.

The sections of the Colorado constitution and statutes that have been cited as possibly raising questions about the legality of public banks are listed here with our opinion on the matter. The research and analysis for our opinion follows in the body of this memorandum.

A. Colorado Constitution

1. The constitution imposes restrictions upon a government lending its credit to another and upon investing in or entering joint ventures with private companies: Article XI, sections 1 and 2.

Article XI, section 1 of the constitution prohibits the state and political subdivisions from lending their credit to a private person or company, unless such measure is for a public purpose. A public bank would not violate that section because lending one's credit is not the same as lending money, and if lending one's credit, i.e. guaranteeing the loan of another, is done for a public purpose, it is not prohibited.

Article XI, section 2 prohibits the state and political subdivisions from making grants or donations to a private company, or entering a joint venture with a private company, unless such measure is for a public purpose. A public bank would not be making grants or donations to private companies, and any loans to private companies or parties would be for a public purpose.

2. The constitution's Article XI restrictions on government debt: Article XI, sections 3, 4, and 6.

Article XI, section 3 prohibits the state from borrowing by loan or in any other form, except for certain limited purposes, namely erect buildings for state use.

Article XI, section 4 prohibits the state from borrowing money unless an irrepealable tax is passed to ensure full repayment.

Article XI, section 6 prohibits political subdivisions of the state from contracting general obligation debt by loan unless an irrepealable tax is passed to pay the loan in full, except for home rule communities whose charters don't require a vote of the people for such purpose.

Sections 3, 4, and 6 of Article XI, do not prohibit public banks, although as we will show, they may have some effect on the ability of the state or a political subdivision to borrow from its own public bank when needed or to borrow money for large projects.

3. TABOR Restrictions on government debt: Article XX, section 20 (4)(b).

Article X, section 20 (4)(b) of the constitution's TABOR Amendment prohibits the state or political subdivision from contracting multiple-fiscal year direct or indirect debt without adequate present cash reserves pledged irrevocably and held for all payments. A public bank operated as an "enterprise" would be exempt from that provision because the term "district" which means the state or a political subdivision as defined in Article X, §20 2(b), expressly excludes enterprises.

4. **The TABOR Amendment's restrictions on revenue and expenditures of the state and political subdivisions, which are defined as "districts," would not apply to a public bank provided it is operated as a self-sustaining enterprise.**

Establishing a public bank as a TABOR enterprise in compliance with Article X, section 20 (2)(b) of the TABOR Amendment would exempt the bank from the TABOR restrictions on revenue and expenditures.

5. The constitution may allow home rule cities and towns in Colorado to establish their own public banks.

Colorado constitution Article XX, sections 1, 4, 5, and 6 - Home Rule for Cities and Towns - authorizes home rule cities and towns to pass laws that don't conflict with state laws of statewide concern, which would appear to permit public banks.

6. Can home rule counties in Colorado establish their own banks?

Colorado constitution Article XIV, §16 (4) provides that state statutes may grant home rule counties any powers that are not prohibited or limited by charter or the constitution. Therefore, the state legislature could authorize home rule counties to establish their own public banks.

B. Colorado Statutes

1. Can a public bank obtain a charter as an LLC in Colorado?

C.R.S. § 11-102-104 (5.5) (a) provides that a limited liability company (LLC) as defined in CRS §7-80-102 may apply for and obtain a Colorado bank charter.

C.R.S. §7-80-203 provides that one or more persons may form an LLC and the persons need not be individuals.

C.R.S. § 7-80-204 (d) (III): An LLC's articles of organization must provide that it has at least one member.

Neither the Colorado constitution nor state legislation contains a restriction on a home rule city or town owning and operating an LLC.

2. Can a public bank obtain a charter as a banking corporation in Colorado?

C.R.S. §11-103-301 provides that five or more individuals as incorporators may apply for a charter as a bank in Colorado, each having paid in cash for 1% or more in par value of the capital and paid in surplus of the bank. Perhaps the state or local government could use that provision through its employees, although at best it would be awkward.

3. A public bank must be an eligible depository under Colorado law. Can a public bank of the state or of a local government meet these provisions?

C.R.S. §11-10.5-106 states that a bank must be a member of the FDIC in order to be an eligible depository for public funds, which are defined as deposits from a governmental unit such as the state, city, town, or county.

C.R.S. § 11-10.5-107 provides that a bank must have 102% collateral for its deposits of public funds.

C.R.S. §24-75-603 provides that it is lawful for cities, counties, and banks to place deposits in certain depositories, including those with 102% collateral for its deposits.

C.R.S. § 11-103-304 provides that when the banking board grants a charter it shall make it contingent upon the bank applying for membership in the Federal Reserve or the F.D.I.C.

Discussion and Analysis

A. Constitutional Provisions.

I. Article XI, §1, which prohibits the state and political subdivisions from lending their credit to another party does not prohibit them from lending money or operating a bank.

Article XI, Section 1 of the Colorado Constitution, "Pledging Credit of State, County, City, Town or School District Forbidden," reads as follows:

Neither the state, nor any county, city, town, township or school district shall <u>lend or pledge the credit or faith thereof</u>, directly or indirectly, in any manner to, or in aid of, any person, company or corporation, public or private, for any amount, or for any purpose whatever; <u>or become responsible for any debt, contract or liability</u> of any person, company or corporation, public or private, in or out of the state. (emphasis added) (effective August 1, 1876, see L. 1877, p. 60.)

First, we will examine the section to determine the plain meaning of the words and whether they appear to prohibit a city from lending money to any person or corporation, public or private. Then we will briefly look at the origin and history of this provision and similar provisions enacted in some 45 states. Finally, we will examine Colorado cases to see how they interpret this section and whether they provide any authority for concluding that the section prohibits the city from operating a bank or lending money.

1. Plain meaning of words in section. A careful reading of the entire section reveals that it does not mention the word "money" or "lending of money**,**" nor does it expressly or impliedly prohibit the state or any political subdivision from lending "money". It only states that the city cannot "lend or pledge" its "credit or faith" directly or indirectly, to another person, company or corporation, public or private, or become responsible for the debt or obligation of another person. The verbs "lend" and "pledge" have as their objects the nouns "credit" and "faith".

So we need to ask what it means to "lend or pledge" one's "credit or faith" to another. *Merriam Webster* online provides a definition of the word "lend" that appears to fit this context as follows: "to make (something) available to (someone or something)." Using this meaning, the section prohibits the city from making its credit available to another person, company, or corporation, public or private.

We next consider the definition of the word "credit". The first online definition of "credit" that comes up in a Google search appears to apply to this situation:

noun: credit
1. the ability of a customer to obtain goods or services before payment, based on the trust that payment will be made in the future.

In order to make its credit available to another, the state, city, or county would need to guarantee a loan, or co-sign a loan to another party, or perhaps agree to indemnify another party against a loss caused by the party to whom the credit is loaned or pledged.

When a government entity guarantees a loan, the lender is relying upon the "loaned" credit of that entity instead of solely upon the credit of the borrower. The term "lend one's credit" or "pledge one's credit or faith" would thus appear to apply to a situation where a city (or other governmental unit) uses its good credit, that is, its ability to obtain a loan, to enable another person to obtain a loan or other benefit, such as by guaranteeing payment of a loan made to that person.

2. The origin and history of state constitutional prohibitions against lending a government's credit to private parties shows they do not prohibit lending money or banking.

The problems addressed by Colorado's constitution Article XI, §1 and 2 were the subject of an A.L.R. report. At 152 A.L.R. 495 it was stated:

> Early in the nineteenth century it seems to have been the general practice of states to encourage the building of railroads by permitting the state or a subdivision thereof to purchase stock in railroad corporations, to issue bonds or lend credit in aid of railroads, or to make outright donations to them. However, due to the large

> number of insolvencies of railroads, caused by frauds or economic conditions, states and subdivisions thereof found themselves largely indebted, and were themselves occasionally insolvent because of large investments in such enterprises. Therefore, a reversal of policy set in. As early as 1851 Ohio adopted a constitution containing a provision prohibiting stock subscriptions or other forms of aid to corporations. In the ensuing twenty-five years most of the other states adopted similar provisions, either prohibiting aid altogether or requiring a vote of the people before a subscription to stock or other sort of aid could be made or extended. At present, at least thirty-eight states have such constitutional provisions, and several have statutory provisions on the subject.

A later updated summary of the early 19th century origin of state constitutional prohibitions against lending the credit of the state or its political subdivisions to private parties or investing in enterprises jointly with private parties is found in the article: "State Constitutional Provisions Prohibiting the Loaning of Credit to Private Enterprise--A Suggested Analysis," 41 *U. Colo. L. Rev.* 135-151 (1969), by Arthur P. Roy. As a result of the failure of such investments, especially in private railroads, 45 states, including Colorado, as of that time had enacted provisions to prevent states and cities from lending their credit to private corporations, such as by guaranteeing such obligations, and from engaging in joint ventures with private corporations. (See list of states at 136-137)

When the State of Colorado was created in 1876, it included the protection against lending the state's or a political subdivision's credit in its Constitution as Article XI, section 1, and its protection against engaging in joint enterprises with private corporations in Article XI, section 2. Section 1 has remained unchanged ever since. Colorado's provision is comparable to those in other states although it is broader in scope and its restrictions are more specific.

These types of restrictions generated "considerable litigation challenging programs which effectuate a partnership between public and private capital… the vast majority" of which involved municipal corporations (Roy, *supra*, at 135). The author stated:

From this historical background, it is evident that the purpose of this provision was to protect the property tax base from debts resulting from private mismanagement by preventing private speculation with public funds (p. 138).

The author goes on to cite numerous cases decided in Colorado and other states, all of which reflect a common purpose to prevent government from lending its credit to private enterprises, except when done for a public purpose. The Colorado cases clearly distinguish between lending money to a private party and lending one's credit to a private party.

3. Federal due process underlies these state constitutional lending and aid restrictions.

In 1874 the U.S. Supreme Court in *Citizens' Savings & Loan Association v. Topeka*, 87 U.S. 655, 659 (1874) declared that there can be no lawful taxation which is not for a public purpose.

In *Green v. Frazier*, 253 U.S. 233 (1920) the U.S. Supreme Court applied the principle declared in *Topeka* to the states, whereby when government money is used in connection with a private project or party it must be used for a public purpose:

> Before the adoption of the Fourteenth Amendment this power (taxation) of the State was unrestrained by any federal authority. That Amendment introduced a new limitation upon state power into the Federal Constitution. The States were forbidden to deprive persons of life, liberty and property without due process of law….

The due process of law clause contains no specific limitation upon the right of taxation in the States, but it has come to be settled that the authority of the States to tax does not include the right to impose taxes for merely private purposes. 253 U.S. at 238.

During the 19th century, a number of states had publicly-owned banks. The drafters of the Colorado Constitution and other state constitutions could easily have added language to prohibit a state or political subdivision from operating a bank or from lending money. The fact that they did not do so makes it apparent that they did not intend to prohibit states from operating banks or from joint ventures with private companies, to which an exception has been established by case law when the operation is undertaken to achieve a public purpose.

4. Colorado Case Law. Numerous Colorado cases have interpreted Article I, section 1. These cases make clear that the prohibition applies only to the lending of the city's "credit" to another party. It prohibits the state and political subdivisions from guaranteeing or co-signing a loan made to a third party. None of the cases suggests that the section might prohibit the entity from operating a bank or lending money to another party.

In *Mayor v. Shattuck*, 34 P. 947 (Colo. 1893) the Supreme Court clearly follows this interpretation of Article XI, §1 as follows: "This section is to be construed as prohibiting a town, or city by its own voluntary corporate act from pledging its credit to, or becoming responsible for, any debt, contract, or liability, in aid of a *third party*."

In the case *Bd. of County Comm'rs v. Humes*, 356 P.2d 910, 910 (Colo. 1960) the Colorado Supreme Court held that a county may not be a guarantor and that Article XI, section 1 of the constitution prevents the county from standing in the position of a guarantor for the debts of an individual.

In *Witcher v. Canon City*, 716 P.2d 445, 448 (Colo. 1986) the Colorado Supreme Court held that "there was no pledge by the City of its credit" and thus the prohibition against lending its credit was not violated. The Court held:

> Here, the contractual obligation to third parties for the construction of the improvements to the Royal Gorge Bridge is solely that of the Company and not the City. Although the City is participating in the modernization by allocating to the project a portion of the tax and toll revenue generated by it, this does not constitute an unconstitutional pledge of the City's credit to the Company. (716 P.2d at 454)

This case also confirms that the prohibition is directed against using the city's credit to aid a third party and is not violated when the sole obligation is that of a private company.

In the case *In re Colorado State Senate etc.*, 566 P.2d 350, 356 (Colo. 1977) the Supreme Court held: "When no debt or obligation of the state is created, the state cannot be said to have lent its credit in violation of article XI, section 1." The Court also held that a proposed appropriation did not violate this section. In that case a proposed house bill appropriation was to be deposited in a capital reserve fund to secure obligations of the housing finance authority. The Court held that the appropriation did not constitute a pledge of the state's credit in violation of this section. Moreover, in the case the housing finance authority is the lender. The housing finance authority is one of a number of examples of the state or a political subdivision of Colorado lending money, with no suggestion that such lending violates Article XI, section 1, which only prohibits lending the "credit" of the state or political subdivision, not the lending of "money".

In *Bradfield v. City of Pueblo*, 354 P.2d 612, 618 (Colo. 1960) the Court held: "The bonds here are those of the City. Art. IX, Sec. 1, cannot be so construed as to keep the state or any subdivision thereof from pledging its own credit for its own debts or obligations as may be permitted by law…." Thus, a city-owned bank could "lend its credit" to guarantee a loan made to the city.

5. The case law of other jurisdictions supports this interpretation.

In Utah, a government entity may make direct loans and not be a lender of credit; it would, however, be a lender of credit if it were guarantor of another's debts. Thus, the lending of state funds is not "lending of credit." *Utah Tech. Fin. Corp. v. Wilkinson*, 723 P.2d 406, 412 (Utah 1986). This was from a challenge to an act that allowed UTFC, a state-run entity, to make direct loans to small businesses, with a public purpose of small business development.

In Wyoming, if a city's credit is not itself put at risk, then there is no constitutional prohibition. "This does not prohibit a city from aiding or benefiting a corporation, if its credit is not involved." *Uhls v. State ex rel. City of Cheyenne*, 429 P.2d 74, 83 (Wyo. 1967).

Similarly, in Michigan, the purpose of the constitutional prohibition against the lending of credit by the state is "to ascertain that the state, which generally cannot borrow, does not accumulate unauthorized debts by guaranteeing the debts of others." M.C.L.A. Const. Art. 9, § 18; *Wayne Cty. Bd. of Comm'rs v. Wayne Cty. Airport Auth*., 253 Mich. App. 144, 658 N.W.2d 804 (2002). Note that Michigan's constitutional prohibition against lending of credit contains a specific caveat within the clause: The Michigan Constitution provides that "[t]he credit of the state shall not be granted to, nor in aid of any person, association or corporation, public or private, except as authorized in this constitution." Const. 1963, art. 9, § 18. And again, in Utah, lending of credit is prohibited by the state constitution if the state acts as a surety or guarantor of another's debts. *Healthcare Servs. Grp., Inc. v. Utah Dep't of Health*, 2002 UT 5, 40 P.3d 591.

The threshold might be whether there is a "binding obligation" on the government entity. Thus, Utah again: "If the legislation requires future appropriations to defray the obligations of the Agency it would be invalid as lending the state's credit, but where, as here, it merely allows future appropriations without requiring such, it creates no binding obligation upon the state and therefore does not result in a debt of the state or the lending of the state's credit." *Utah Housing Finance Authority v. Smart*, 561 P.2d 1052, 1056 (1977).

In conclusion, the plain meaning of the words in Article XI, section 1, the original purpose and history of the section, and Colorado case law make clear that the prohibition against lending or pledging the credit of a city, i.e. its ability to pay its obligations, to another person or entity applies solely to cases in which the city guarantees or otherwise assumes the obligation of another party. There is no indication that it would prohibit a city from lending money to third parties or to itself or from operating a public bank.

II. Article XI, §1 permits the city to "lend its credit" to another for a public purpose.

As shown below, Colorado has relaxed the requirement of Article XI §2 of its Constitution to permit a city to give aid to a corporation or company or enter a joint venture with a corporation or company provided it fulfills a "public purpose." In the law review article discussed above, Mr. Roy states:

"It is not uncommon for a court to rule that the credit lending provisions do not prohibit aid to state agencies such as port authorities, housing authorities, etc., but most such cases turn more on public purpose than the nature of the recipient. Based on the narrowly defined purposes of the credit lending provisions, aid to governmental units, where a direct benefit is realized by the assisting governmental unit, should be outside the credit lending prohibitions." (41 U. Colo. L. Rev. 135 at 149-150) *Orbison v. Welsh*, 179 N.E.2d 727 (Indiana 1962) (the funds to repay the bonds of the Indiana Port Commission were to come from revenue of the Commission, a separate entity from the state and did not obligate the state. Therefore, they did not violate the constitutional provision against the state contracting a debt).

The Bank of North Dakota (BND) regularly lends its credit to private community banks through guarantees of loans it makes jointly with community banks, and also through letters of credit to back such loans. These actions facilitate the loans and help achieve a lower interest rate. Such practice has made North Dakota's community banks stronger and reduced the risk of default on such loans. Evidence of the benefits of such guarantees to the state of North Dakota is abundant: for many years the state has had no bank failures. It also has had the lowest unemployment rate, one of the lowest home foreclosure rates, and the lowest credit card default and student loan default rates in the country. It has by far the highest number of community banks per capita. Further, the BND has achieved an average 18% return on equity over the past 16 years.

Assuming home rule cities and counties or the state of Colorado were to establish public banks with a structure and practices comparable to the BND, a solid case can be made that lending their credit by guaranteeing loans or providing letters of credit to local private community banks would provide substantial public benefit to their local communities by strengthening the ability of the community banks to make loans to small and medium sized business, agriculture, student loans, loans for education, affordable housing, clean energy, health services in underserved areas, environmental cleanup, and other public purposes. By lending its credit to these banks with loan guarantees, and lending a little more in an economic decline, the BND prevented any recession from occurring in 2008 and after. A public bank would thereby create many well-paying jobs and a strong and stable local economy, just as the BND has done in North Dakota for the past 100 years. Additional sources of public benefit are that a state, city, or county public bank, like the BND, after approval of the loan by a private community bank, would review the loan applicant's credit worthiness and the nature and terms of the loan before agreeing to back the loan, thus creating a second level of review for greater protection. Therefore, many compelling grounds exist for the Colorado courts to find a "public purpose" exception to the prohibition on the state, city, or other political subdivision lending its credit to a private business or person through its own public bank.

Other jurisdictions support the public purpose exception. In these lines of case law, a policy is buffered from constitutional criticism regarding the lending of credit *at the point that such an act is identified with a "valid," "strong," or otherwise qualified public purpose.* Because of this, it should be emphasized that there is strong precedent to allow government entities to function, essentially, as lenders and as guarantors of loans.

Both constitutional prohibitions—against the lending of credit and against "gifting"—are put aside if the policy serves a public purpose. See, e.g., *State ex inf. Danforth ex rel. Farmers' Elec. Co-op., Inc. v. State Envtl. Improvement Auth*., 518 S.W.2d 68, 75 (Mo. 1975) ("Even if the activities of the Authority, in receipt and disposition of funds, were to be construed as a 'lending of credit' or 'grant of public money,' the same would not be proscribed by §§23 and 25 of Art. VI of the Missouri Constitution in view of the obvious 'public purpose.'").

Similarly, in Utah, a "Housing Finance Agency Act" served a public purpose "to alleviate an actual and existing problem having significant affect (sic) upon the public health, safety, and welfare." *Utah Hous. Fin. Agency v. Smart*, 561 P.2d 1052, 1054 (Utah 1977). This public purpose construal was sufficient to rebuff a constitutional challenge based on the Finance Authority essentially acting as a bank in lending money to private entities. The Act permitted the Agency to obtain funds from notes and bonds (essentially the capitalization of its banking capacity) and then to make those funds "available on a low interest basis for the financing of the purchase, construction, or rehabilitation of housing for low and moderate income persons." 561 P.2d at 1053. The court wrote:

> The Agency may adopt a number of techniques for making its funds available. It may make direct loans through qualified mortgage lenders to individuals for purchase, construction, or rehabilitation of housing. It may create a housing rehabilitation fund for direct loans for rehabilitation of low and moderate income housing. It may make loans to local housing authorities for purchase or construction of low and moderate income housing. It may purchase loans from qualified mortgage lenders, providing that the funds paid the lender by the Agency will be used by the lender to make low interest mortgages to low and moderate income persons as defined by the Agency. *Id*. at 1053.

The court pointed out that "[m]any states with similar statutes have held that a public purpose is served by similar provisions for low income housing acts." *Id.* (citing *California Housing Finance Agency v. Elliott*, 551 P.2d 1193 (Cal. 1976); *Rich v. State of Georgia,* 227 S.E.2d 761 (Ga. 1976); *In re Constitutionality of ORS 456.720 v. Smith,* 537 P.2d 542 (Or. 1975); *West v. Tennessee Housing Dev. Agency,* 512 S.W.2d 275 (Tenn. 1974); *Vermont Home Mortgage Credit Agency v. Montpelier National Bank*, 262 A.2d 445 (Vt. 1970)). Nearly all such housing acts call for government entities to function as lending authorities.

Construed broadly*:* Beyond just the lending of credit, "public purpose" is also to be broadly construed in most jurisdictions in general, and broad construal appears to be the consensus of legal scholars. *Dannheiser v. City of Henderson*, 4 S.W.3d 542, 546–47 (Ky. 1999) "Other municipal text writers have correctly stated that 'public purpose' should be broadly construed to comport with the changing conditions of modern life." (citing Eugene McQuillen, *The Law of Municipal Corporations*, § 39.19).

Similar expressions of the breadth of public purpose doctrine may be found in New Hampshire, *Opinion of Justices*, 288 A.2d 697 (N.H. 1972); Kansas, *Duckworth v. City of Kansas City*, 758 P.2d 201 (Kansas 1988); Oklahoma, *Burkhardt v. City of Enid*, 771 P.2d 608 (Okla.1989); Oregon, *Carruthers v. Port of Astoria*, 438 P.2d 725 (Or. 1968); South Dakota, *Clem v. City of Yankton*, 160 N.W.2d 125 (S.D.1968); Florida, *Linscott v. Orange County Industrial Development Authority*, 443 So.2d 97 (Fla. 1983); Delaware, *In re Opinion of Justices*, 177 A.2d 205 (Del.1962); Connecticut, *Roan v. Connecticut Industrial Building Comm.*, 189 A.2d 399 (Conn. 1963); *Wilson v. Connecticut Product Development Corp*., 355 A.2d 72 (Conn. 1974); and Nebraska, *Chase v. County of Douglas*, 241 N.W.2d 334 (1976).

"If an act serves a public purpose it will not be inconsistent with constitutional prohibition against the lending of credit or the appropriating of money by a municipality to any person notwithstanding the fact that the proceeds or profit may inure as a result of the act to a private individual." *Fraternal Order of Firemen of Wilmington, Del., Inc. v. Shaw*, 196 A.2d 734 (Del. 1963).

Reasonable construction is sufficient; strict scrutiny is not required. Finally, it is important to note that reasonable construction is sufficient: a court will not strictly evaluate whether the policy meets its intended public purpose goal. The Kentucky example shows how public purpose exceptions are not strictly scrutinized: "the City must only prove that the development bears a reasonable or sufficient relationship to the purpose of economic growth. As long as there is a sufficient relation to the accomplishment of a legitimate public purpose, there is no necessity for the courts to interfere with the determination of public purpose." *Dannheiser*, 4 S.W. 3d at 548.

Public welfare*:* The Ohio Const. art. VIII, § 6 provides in part:

No law shall be passed authorizing any county, city, town or township, by vote of its citizens, or otherwise, to become a stockholder in any joint stock company, corporation, or association whatever; or to raise money for, or <u>loan its credit to</u>, or in aid of, any such company, corporation, or association." (emphasis added)

The Ohio Supreme Court, in *State ex rel. Tomino v.* Brown, 549 N.E.2d 505, 508 (Ohio 1989), considered the constitutionality of an ordinance that called for the construction of subsidized housing for individuals and thus involved the *lending of the credit* of the city to enable the purchasers to buy the houses. The Respondent, Director of Finance for the city of Cleveland had refused to approve the certificates for payment, contending that the transaction may violate the above provision of the constitution as an unlawful lending of the city's credit in aid of private parties. The Court granted a writ of mandamus to compel the issuance of the certificates, holding as follows: "We find that there will be a lending of the city's credit to purchasers of the units. However, since this lending of credit is for a public welfare purpose, and not a business purpose, it is not prohibited by Section 6 of Article VIII."

Risk under public control. In the state of Washington, if risk to taxpayers remains under public control in the execution of lending for a public purpose, there is no constitutional violation concerning the state's credit. *Washington State Hous. Fin. Comm'n v. O'Brien*, 671 P.2d 247, 251 (Wash. 1983). The Supreme Court stated:

Relief of unemployment is a valid public purpose even if the state incurs indebtedness. *Hayes v. State Prop. & Bldgs. Comm'n*, 731 S.W.2d 797, 800 (Ky. 1987) (citing *Industrial Development Authority v. Eastern Kentucky Regional Planning Com.*, 332 S.W.2d 274, 277-78 (Ky. 1960).

Environmental quality: Environmental improvement loans in Missouri did not violate constitutional prohibition against lending of credit. "Even if the activities of the Authority, in receipt and disposition of funds, were to be construed as a 'lending of credit' or 'grant of public money,' the same would not be proscribed by §§ 23 and 25 of Art. VI of the Missouri Constitution in view of the obvious 'public purpose.'" *State ex rel. Danforth v. State Envtl. Improvement Auth*., 518 S.W.2d 68, 75 (Mo. 1975). Environmental quality is a public concern. *Annbar Associates v. West Side Development Corp*., 397 S.W.2d 635 (Mo. banc 1965).

If for the Benefit of the State: Both Virginia and Kentucky courts have reasoned that when the underlying purpose of a government transaction involving a financial obligation is to benefit the State, *even when the state incurs debt as a result*, the constitutional prohibition against lending the State's credit is not violated. See *Almond v. Day*, 91 S.E.2d 660, 667 (Va. 1956) "Merely because the State incurs an indebtedness or expends its funds for its benefit and others may incidentally profit thereby does not bring the transaction within the letter or the spirit of the 'credit clause' prohibition."

Public Purpose is Always Changing: Public purpose is constantly changing. *Laret Inv. Co. v. Dickmann,* 134 S.W.2d 65, 68 (Mo. 1939):

To be guided solely by whether a given activity had, at some previous time, been recognized as a public purpose would make the law static. Such a standard would compel us to retain in the law, as appropriate for public expenditure, activities which have ceased to be of public concern; and would prevent us from adopting new public functions regardless of how essential to the public welfare they may have become by reason of changed conditions." *State v. Land Clearance for Redevelopment Auth.*, 270 S.W.2d 44 at 50 (Mo. *en banc* 1954).

Public Purpose, "Donations and Grants," and Public Bank Below-Market Interest Rates: On its face, a public bank *lends* money; this lending comes with an intrinsic or definitional expectation; the loan has legitimate components: principal, interest, and collateral, the promise to repay it, and to pledge collateral to secure repayment. The purpose, on the other hand, of the constitutional prohibition against donations and grants, is "to prohibit the state or a political subdivision from transferring public funds to a private company or corporation *without receiving any consideration in return.*" *City & Cty. of Denver v. Qwest Corp*., 18 P.3d 748, 758 (Colo. 2001) (emphasis added) (citing *City of Aurora v. Pub. Utils. Comm'n*, 785 P.2d 1280, 1288 (Colo. 1990); *Lord v. City & County of Denver*, 143 P. 284 (Colo. 1914) (holding that an agreement by the City and County of Denver to aid a railroad company in connection with the construction of the Moffat Tunnel violated Article XI, section 2); *Colo. Cent. R.R. Co. v. Lea*, 5 Colo. 192 (1879) (invalidating agreement under which Boulder County planned to transfer 2,000 shares of stock to a railroad upon the railroad's completion of an extension of its line to Cheyenne, Wyoming)). *See also Northlake Marine Works, Inc. v. City of Seattle*, 857 P.2d 283 (Wash. App. 1993) ("In order to determine whether gift has occurred in violation of constitutional prohibition against gifts of public property and lending of credit, it is necessary to find that property has been transferred with donative intent and without consideration; if donative intent cannot be proven, adequacy of consideration will not be closely scrutinized, but assessed for legal sufficiency") (citing West's RCWA Const. Art. 8, § 7).

Absent the public purpose exception, there is a scenario where a public bank might be thought to be subject to the constitutional prohibition on donations and grants. This objection would stem from the public bank's ability to lend at below-prevailing-rate interest. A public bank that lends at an interest rate that is "below market value" may arguably be subject to the charge of making a "donation or grant in aid." Fair market value is a common test or threshold for the conferral of a "donation or grant in aid." See *Denver Urban Renewal Auth. v. Byrne*, 618 P.2d 1374, 1383-84 (Colo. 1980) (citing *Chitwood v. City and County of Denver*, 201 P.2d 605, 608 (Colo. 1948).

But the public purpose exemption justifies policies like a public bank lending at lower interest rates than the private banking norms of the moment. Even if the actions of a government entity result in a monetary benefit being conferred upon a private entity, Art. XI sec. 2 does not bar such conferral if it is associated with action that furthers a valid public purpose. *City & Cty. of Denver v. Qwest Corp*., 18 P.3d 748, 758 (Colo. 2001).

One example that Colorado courts see as being compatible with a public purpose are urban renewal projects, which Colorado sees as serving such a "strong public purpose." See *Denver Urban Renewal Auth. v. Byrne*, 618 P.2d 1374, 1383-1384 (Colo. 1980) (no violation of Colo. Const. Art. XI, §2; citing *Pillar of Fire v. DURA*, 509 P.2d 1250 (Colo. 1973).

Therefore, even if a bank's lending function is not enough to resist charges that a public bank is a government entity conveying a gift, grant, or donation (where such a charge would stem from public bank's ability to lend at extremely low interest), the public purpose exception allows such conferring of benefit to a private entity in the furtherance of a strong public purpose—like urban economic development.

II. Article XI, §2 Prohibition Against Donations, Grants, or Joint Ownership

1. Article XI, § 2, "No Aid to Corporations - No Joint Ownership by State, County, City, Town, Or School District," reads as follows:

> Neither the state, nor any county, city, town, township, or school district shall make any donation or grant to, or in aid of, or become a subscriber to, or shareholder in any corporation or company or a joint owner with any person, company, or corporation, public or private, in or out of the state, except as to such ownership as may accrue to the state by escheat, or by forfeiture, by operation or provision of law; and except as to such ownership as may accrue to the state, or to any county, city, town, township, or school district, or to either or any of them, jointly with any person, company, or corporation, by forfeiture or sale of real estate for nonpayment of taxes, or by donation or devise for public use, or by purchase by or on behalf of any or either of them, jointly with any or either of them, under execution in cases of fines, penalties, or forfeiture of recognizance, breach of condition of official bond, or of bond to secure public moneys, or the performance of any contract in which they or any of them may be jointly or severally interested. Nothing in this section shall be construed to prohibit any city or town from becoming a subscriber or shareholder in any corporation or company, public or private, or a joint owner with any person, company, or corporation, public or private, in order to effect the development of energy resources after discovery, or production, transportation, or transmission of energy in whole or in part for the benefit of the inhabitants of such city or town. (emphasis added) (Colo. Const. Art. XI, Section 2) (emphasis added)

The above section contains several prohibitions and an express authorization for energy purposes, which we will evaluate as to whether they either prohibit or allow a home rule city or county to own and operate a corporation or LLC chartered as a bank in Colorado. We will discuss these provisions one at a time.

Clarifying the terms "public" and "private." At the outset of this memorandum we defined a "public" bank as a bank owned and operated by government. However, as commonly used in regard to a corporation, "public" refers to a corporation or company whose stock or certificates of ownership are sold publicly to any would-be buyer on the stock market or other public market, as opposed to a "private" sale of stock to someone known to or approved by the seller. As used in the above Article XI, §2, the term "public" refers to stock or interests sold publicly on the stock market or other public market, and not to government ownership, and the term "private" refers to a company whose stock or ownership interests are not sold to the public on a stock market or similar public venue. Thus, as correctly understood, Article XI, §2 prohibits government investment in non-government owned businesses. Thus, for example, Article XI, §2 does not prohibit a city from owning and controlling 100% of a bank, i.e. a "public bank" as defined herein. To avoid confusion, when we use the terms "public" and "private" herein we will make clear which definition of those words we are using.

Prohibition on donations and grants: Article XI, section 2 prohibits the state, city, county, town, township, or school district from making a donation or grant to a private person, corporation, or company. Because a borrower must pay back the principal and any interest, an ordinary loan by a bank is not a grant or donation. Therefore, this language clearly would not prevent a city from lending money or operating a bank.

Prohibition of stock ownership, or joint ownership with a privately-owned corporation or company: Using the term "public" as clarified above, Article XI, §2 prohibits the state, and political subdivisions from subscribing to or owning interests in a privately owned corporation, and from joint ownership with such entity, "except as to such ownership as may accrue to the state" in a variety of specified circumstances, each of which involves a public benefit conferred upon or received by the government, such as by force of law, or when a governmental unit is the passive recipient of the private interest. Article XI, §2 does not appear to prohibit a governmental entity from owning and controlling 100% of a corporation or company because with such ownership it would not own any interest in a privately-owned corporation.

Public purpose exception. Furthermore, Colorado case law eventually established that conferring a benefit upon a private corporation is not prohibited as long as the project is for a "public purpose." *In re Interrogatory Propounded by Governor Roy Romer*, 814 P. 2d 875, 882 (Colo. 1991). In that case, although the bill in question did not specifically mention United Airlines, it was clear that the bill if passed would facilitate the construction of a maintenance facility for airplanes that all parties acknowledged would benefit United Airlines and presumably enable it to stay in Denver. However, the bill also would create many new jobs at substantial pay, and thus give a boost to the Colorado economy. The Supreme Court of Colorado held that despite the benefit to a major airline corporation, the bill served a "public purpose" and thus did not violate Art. XI, § 2 of the Constitution. The court relied upon a long line of Colorado cases in which private corporations or parties were benefited by legislation, but which the Court upheld as constitutional because it served a public purpose.

The court in *Romer* stated: "At first this prohibition of aid to corporations, absent consideration, was strictly enforced," citing *The Colorado Central R.R. v. Lea,* 5 Colo. 192 (1879) in which the court declared null and void a donation of 2,000 shares of stock belonging to Boulder County, to the Colorado Central Railroad Company. The Court in *Romer* then stated: "Notwithstanding the apparent absolute prohibition of article XI, section 2, a 'public purpose' exception has evolved," citing *McNichols v. City & County of Denver,* 280 P.2d 1096 (1955), which upheld an ordinance establishing a retirement program for city employees based upon the plan's "public purpose". 814 P. 2d at 882.

Legislation is presumed to be constitutional, and won't be declared unconstitutional unless established beyond a reasonable doubt. In *Romer* the Court further followed long-standing precedent by holding that "A bill that has been enacted by the General Assembly is 'presumed to be constitutional and cannot be declared unconstitutional unless that conclusion is established beyond a reasonable doubt.'" 814 P.2d at 883.

Thus, Article XI, §2 does not prohibit legislation that benefits a private corporation or company provided that the legislation serves a "public purpose." Therefore, the state, a city, or county may "become a subscriber to, or shareholder in" a "corporation or company or a joint owner" with a "company, or corporation" provided it is for a public purpose. Actually, the state, cities, and counties legally and regularly invest in the stocks of many different companies, typically a small percentage of the company's total stock and a limited percentage of the government's total investments, with no right of control over the company, under state statutes and municipal charters or ordinances that authorize such investments and prescribes rules and limits on such investments. However, a public bank as we envision it would be wholly owned and controlled by the government entity that established it and would not contravene this section. A public bank's loans to private businesses would not involve the bank in becoming shareholder or subscriber in a corporation or company, and they would be made for public purposes, such as create new jobs, increase employment, provide necessary services for the community, increase the tax base, and the like.

We have reviewed numerous court decisions above involving public projects that were objected to as unconstitutional on the ground that they involved lending the government's credit to private companies or that they aided private companies. Those court decisions approved the projects in part on the ground that any lending of credit or aid to private companies was predominantly to serve a public purpose. The standard of review does not require close scrutiny and the cases show that a measure will be approved as long as it appears reasonably related to a public purpose. A public bank would naturally be lending money for similar public purposes---affordable housing, home loans to promote home ownership, infrastructure to serve the community and support the economy, loans to strengthen small businesses and increase employment, construction of hospitals and provision of health care to underserved areas, sustainable agriculture, student loans, educational facilities, lending to support clean energy, and much more. Studies show that major banks do not lend much to small and medium sized businesses, even though small and medium size businesses are where most new jobs are created. Public banks fulfill a valuable public purpose by creating a new source of income without raising taxes. It seems incongruous at best, and highly irresponsible at worst, to assume that we as citizens cannot control and direct our own money in the public interest through establishing public banks, but must turn it over to private parties who have no obligation to the public interest, and whose goal will be to maximize their own profit.

Public banking and public control of money have a well-established history. Attached hereto is a summary describing many successful public banks in America, past and present.

Because a city, county or the state may own an investment in the form of a small percentage of stock of a company, one might ask why, since it is not prohibited, it wouldn't be lawful for such government to own 100% of the stock of a company, assuming it had control of the company in order to ensure that it focuses totally upon serving public purposes and needs.

As explained above, the problem that was addressed in Article I, §§1 and 2 of the Colorado constitution in 1876 was that during westward expansion in the early 1800s many cities were investing money in private railroads whose operations were speculative and risky. Many such railroad and related investments failed, especially in the wake of repeated recessions, such as 1837, and the cities' investments failed with them. Roy, *supra* at 136. As also stated, forty-five states, including Colorado, adopted constitutional provisions prohibiting the lending of credit and investing in private corporate ventures. *Ibid*. The railroad corporations' primary focus was to maximize profit for their shareholders, leading them to take unreasonable risks. In contrast, a corporation or company wholly owned by a city would have as its primary goal to serve the interests of the taxpayers and citizens of the city.

In fact, the most important distinguishing factor between a public bank and a private bank is that a public bank's charter and mission is to serve the citizens and needs of a community, whereas a private bank's goal is to maximize profit for its shareholders. As a result, we saw how the major Wall Street banks took unreasonable risks and engaged in fraudulent and reckless lending to maximize profit. When the economy started to fail, the major banks all reduced their lending and thus contributed to the Great Recession--the worst collapse of the U.S. economy since the Great Depression. In contrast, the Bank of North Dakota, committed to the community, increased its lending modestly in 2008 in partnership with North Dakota's local community banks to offset the decline and as a result achieved record prosperity in 2008 and each year thereafter. North Dakota was the only state not to suffer a serious economic recession in 2008 and after.

Below we discuss whether Article XI, section 2 allows a home rule city or other home rule governmental entity, under the broad authority granted to home rule communities by Article XX §6, to own 100% of a corporation or limited liability company (LLC) that is established to serve public purposes.

Because the purpose of Article XI §2 is to prevent the state or political subdivision from risking its financial condition on investments or joint ventures with private companies, a legislative measure to establish a state owned public bank or to authorize cities, towns, and counties to established public banks whereby the state or political subdivision would own 100% of an LLC and the LLC apples for a charter under Colorado banking law to serve public purposes would not violate Article XI §2.

(2) Article XI, section 2 specifically authorizes cities and towns to own an interest in a private banking company in order to operate an electric utility.

As quoted above, the second sentence of Article XI, §2 reads as follows:

> Nothing in this section shall be construed to prohibit any city or town from becoming a subscriber or shareholder in any corporation or company, public or private, or a joint owner with any person, company, or corporation, public or private, <u>in order to effect the development of energy resources after discovery, or production, transportation, or transmission of energy</u> in whole or in part for the benefit of the inhabitants of such city or town. (emphasis added) (Colo. Const. Art. XI, Section 2)

This section would appear to authorize any city or town to own and operate a public bank "in order to effect the development of energy resources after discovery, or production, transportation, or transmission of energy in whole or in part for the benefit of the inhabitants of such city or town." Such authorizing language appears sufficient to permit such public bank to lend money to a city in order to facilitate the acquisition of ownership of its electric utility and to operate it, or to finance the conversion from fossil fuels to solar, wind, or other sustainable source of energy. The language of the provision expressly authorizes becoming a "subscriber" in "any…company, public or private" in order to "effect the development of energy.…" A limited liability company is a "company" and a city would be a "subscriber" if it purchased 100% interest in an LLC to be chartered and operated as a public bank under Colorado law for the purpose of owning and operating its own electric utility or for funding production, transmission, and distribution of energy by others. Because no publicly owned banks have ever been established in Colorado, no case law exists on the issue. However, the language of the constitutional provision is clear and appears to leave little if any doubt that a city or town could establish a public bank for any purposes related to energy production, transmission, and distribution for its inhabitants.

(3) Would Article XI section 2 prohibit the state and local governments from depositing their money in major Wall Street banks?

Recent developments make this a question worth asking. After the repeal of the Glass-Steagall Act in 1999, the major banks are now allowed to combine their traditionally conservative bank lending operations with their investment banking activities, which often involve taking major risks. The repeal exposes depositors to significant additional risks, such as speculative investments, mortgage backed securities, derivatives, and credit default swaps, such as those that brought down our economy in 2008. The F.D.I.C. only has enough assets to meet a small fraction of the deposits of its customers in the event of another major economic collapse. Many experts say that another bubble is currently being created in real estate, and that the economy is likely to crash again. The Dodd-Frank Act of 2010, enacted as a result of the 2008 crash, provides that if a bank becomes insolvent, it has the right to execute a "bail-in", whereby it may help itself by taking a percentage of each depositor's deposits, say 10%, to restore the bank's solvency.

Because the risk of a bank's failure is now arguably greater than it used to be due to the repeal of Glass-Steagall and the fact that a government's deposits are at greater risk due to the new "bail-in" procedure authorized by Dodd-Frank, a government that places its deposits in a private bank might be deemed to have violated the restriction in Article XI, section 2 that states a government may not invest in private corporations or risk its assets in private ventures. While the government might argue that it did so to serve a public purpose, the availability of a viable alternative of placing a government's deposits in its own public bank and avoiding the substantial risks and adds costs involved in placing its deposits shows the "public purpose" argument would no longer hold for continuing to place its deposits in the "too big to fail" Wall Street banks.

Fiduciary duty of government officials. Scholars in the field of government ethics assert that state, city, and county elected and appointed public officials owe a fiduciary duty to their citizens with regard to the officials' handling of the public's money. e.g. Markkula Center for Applied Ethics at the University of Santa Clara; http://harvardlawreview.org/2013/01/translating-fiduciary-principles-into-public-law/ Now that public officials are aware or should be aware, in the exercise of reasonable care, that they have available an alternative and superior way to manage their assets and finances by establishing public banks, it can rightfully be asserted that it would be a breach of their public officials' fiduciary duty to their citizens to continue to place and risk their deposits in the major banks. Thus, public officials should act responsibly to promptly take the steps necessary to establish their own public banks, including investigating the means of doing so, such as preparing a business plan to create such banks and maximize their effectiveness.

By continuing to place their deposits in major Wall Street banks, the government foregoes the advantages of depositing its liquid assets in its own bank, and thereby of substantially increasing lending in the local community, of borrowing from its own bank at reduced or no interest, of avoiding excessive fees for banking services, and of having a major new source of income without raising taxes. Without a public bank, a government must tax its people in order to repay the bonds required to fund its operations. A public bank would not pay commissions and fees for making loans, would have low overhead, such as no advertising, no tellers or ATM machines, no exorbitant salaries or bonuses for its officers, no dividends, and no branches, and would not make speculative investments or loans. By foregoing all those advantages of public banks and incurring all of the above disadvantages of depositing in major Wall Street banks, it is hard to escape the conclusion that government officials are breaching the public's trust.

3. Article XI, §3, which prohibits the state from contracting debt, does not prevent the state from owning and operating a public bank.

Article XI, §3 of the Colorado constitution "Public Debt of State – Limitations" reads as follows:

> <u>The state shall not contract any debt by loan in any form</u>, except to provide for casual deficiencies of revenue, erect public buildings for the use of the state, suppress insurrection, defend the state, or, in time of war, assist in defending the United States; and the amount of debt contracted in any one year to provide for deficiencies of revenue shall not exceed one-fourth of a mill on each dollar of valuation of taxable property within the state, and the aggregate amount of such debt shall not at any time exceed three-fourths of a mill on each dollar of said valuation, until the valuation shall equal one hundred millions of dollars, and thereafter such debt shall not exceed one hundred thousand dollars; and the debt incurred in any one year for erection of public buildings shall not exceed one-half mill on each dollar of said valuation; and the aggregate amount of such debt shall never at any time exceed the sum of fifty thousand dollars (except as provided in section 5 of this article), and in all cases the valuation in this section mentioned shall be that of the assessment last preceding the creation of said debt (emphasis added).

The above section provides that the state of Colorado cannot borrow money unless taxes are passed concurrently to pay it back. Banks, including public banks, sometimes need to borrow money in order to have the necessary deposits to cover checks drawn on the bank, or to provide reserves to cover new loans, or for other purposes. However, if the bank is a separate entity from the state, particularly if it is operated as a TABOR enterprise, it should not be prohibited from borrowing as long as it is clear that the state is not obligated to repay such loans and has not guaranteed repayment. In addition, the state's deposits in the bank will be backed up by the bank, which is a debtor as to the state's deposits. As a separate entity from the state, the bank's backing of the state's deposits will not involve borrowing by the state.

In addition, proponents' plans for public banks in Colorado call for them to be created as "TABOR enterprises." The banks can then pay back loans out of the interest income it earns on loans and not have to rely upon the government for repayment. Further, a TABOR enterprise is authorized to issue revenue bonds, which could provide a source of income to repay a loan without the state being directly involved. Finally, we contemplate that the bank's deposits will be backed up by 102% collateral through a letter of credit from the Federal Home Loan Bank. That method of protecting deposits also does not require the state to borrow any money. Thus, a public bank will not require the state to borrow money or to violate Article XI, section 3.

3. Article XI, §4, which prohibits the state from contracting debt, does not prohibit the state from owning and operating a public bank.

Article XI, §4, Law Creating Debt, provides as follows:

> In no case shall any debt above mentioned in this article be created except by a law which shall be irrepealable, until the indebtedness therein provided for shall have been fully paid or discharged; such law shall specify the purposes to which the funds so raised shall be applied, and provide for the levy of a tax sufficient to pay the interest on and extinguish the principal of such debt within the time limited by such law for the payment thereof, which in the case of debts contracted for the erection of public buildings and supplying deficiencies of revenue shall not be less than ten nor more than fifteen years, and the funds arising from the collection of any such tax shall not be applied to any other purpose than that provided in the law levying the same, and when the debt thereby created shall be paid or discharged, such tax shall cease and the balance, if any, to the credit of the fund shall immediately be placed to the credit of the general fund of the state.

The term "debt above mentioned in this Article" in the first line of the section just quoted refers to Article XI, section 3, which only concerns debt incurred by the state. Therefore, section 4 means that any debt contracted by the state requires an irrepealable tax measure to pay for it. If a public bank is set up as an independent arm of government, the same arguments that were made in the preceding section with regard to Article XI, §3 should apply. Thus, the state or political subdivision involved would not be incurring debt. Any debt created by the bank would be paid out of the income or revenue from the bank.

3. Article XI, §6, which prohibits political subdivisions of the state from borrowing without enacting a tax to pay it, does not prevent the operation of a public bank.

Article XI, §6, Local Government Debt, provides: "(1) No political subdivision of the state shall contract any general obligation debt by loan in any form" (except by adopting a legislative measure that ensures payment of the debt in full). It also provides that a vote of the people is required to approve any debt unless the charter of a home rule city, county, or town states that voter approval is not required. Debts of home rule communities to supply water are exempted from this section.

Article XI, §6 applies essentially the same conditions to ensure repayment of local government debt that Article XI, §§3 and 4 apply to debt incurred by the state, that is, the requirement for a tax measure, either through legislation or ballot measure. Again, if the public bank is established as an independent government entity and as a TABOR enterprise, the bank will be able to incur debt without the local government being responsible for the debt. Therefore, no tax measure will be required to be approved by the local government or by vote of the people. The public bank, as a TABOR enterprise, can borrow without the need for any new taxes because a public bank has its own source of income in the form of interest on loans that it makes.

As stated above, the TABOR Amendment, Article X, Section 20 of the Colorado constitution, provides that a self-sustaining enterprise is exempt from TABOR restrictions on revenue and expenditures, as long as it complies each year with section 2(d) of TABOR.

A number of Colorado communities, such as the city of Boulder in 1996, have "de-Bruced," that is, made those cities exempt from TABOR restrictions on revenue and expenditures by a vote of the people. Therefore, those cities may not need to establish a public bank as a "TABOR enterprise."

However, for cities and counties that have not de-Bruced, and for the state of Colorado, which has not de-Bruced, it is strongly recommended that any public bank be established as a "TABOR enterprise", as defined in section 2(d) of Article X, Section 20 of the Colorado Constitution, i.e. the TABOR Amendment.

Section 2(d) of TABOR defines the term "enterprise" as:

"a government owned business authorized to issue its own revenue bonds and receiving under 10% of annual revenue in grants from all Colorado state and local governments combined."

Each part of the definition must be met each year to qualify as a TABOR Enterprise for the following year, in which case the enterprise is exempt from TABOR income and expenditure limits. A self-sustaining, well-run public bank should easily be able to meet the "under 10%" of annual revenue requirement each year. Nonetheless, it might want to set aside a portion of its income annually to build up a moderate sized rainy-day fund in the event the bank should ever suffer an annual loss. It could then use a portion of the fund to help cover the loss so as to ensure that less than 10% of its income comes from state government for the year involved. This positive assessment is supported by the fact that the Bank of North Dakota has achieved an average return on equity of 18% over the last 16 years. The other requirements that must be met each year to be a TABOR enterprise--publicly owned and authorized to issue revenue bonds should not be an issue because the enabling legislation would expressly provide that the bank be publicly owned and operated, and would authorize it to issue its own revenue bonds. TABOR section 2(d) does not require that the enterprise actually issue revenue bonds. However, revenue bonds would be one effective way to either create or expand the lending power of the bank. The high profitability of professionally managed public banks would ensure that the revenue bonds would be timely repaid. Thus, compliance with the TABOR enterprise requirements to ensure that the bank's income and expenditures would be exempt from TABOR limits could be readily achieved, year after year.

4. Article X, §20 (4)(b) of the TABOR Amendment, which prohibits the state and local governments from multi-year borrowing would not apply to a public bank operating as a TABOR enterprise.

Article X, §20 (4)(b) of TABOR prohibits any "district", that is, the state and any local government, from creating "multiple-fiscal year" debt, except to refinance existing bonds at a lower interest rate or to add new employees to existing pension plans, unless the government has "voter approval in advance" and the government has "adequate present cash reserves pledged irrevocably and held for payments in all future fiscal years."

Section 2(b) of TABOR defines "district" as "the state or any local government, excluding enterprises." Therefore, by definition a public bank established as an "enterprise" is expressly excluded from the operation of subsection 4(b) and would not be subject to the restriction on multi-year borrowing.

7. Are the home rule provisions of Articles XX and XIV of the Colorado constitution broad enough to allow rule cities and counties to establish their own banks?

Article XX, section 6, Home Rule for Cities and Towns authorizes home rule cities and towns to pass laws that don't conflict with state laws of statewide concern. Article XIV, section 16 (1) provides that counties may also adopt home rule.

Home Rule Cities and Counties in Colorado May Own and Operate Their Own Banks

We have not found any provision of the Colorado constitution or legislation specifically mentioning or authorizing the establishment of a city-owned or other public bank. However, Article XX of the Colorado Constitution, grants home-rule powers to cities and towns operating under its provisions. CO. CONST. Art. 20 § 6. Section 6 provides very broad authority to home rule cities. It states that home rule cities:

> always have, power to make, amend, add to or replace the charter of said city or town, which shall be its organic law and extend to all its local and municipal matters.
>
> Such charter and the ordinances made pursuant thereto in such matters shall supersede within the territorial limits and other jurisdiction of said city or town any law of the state in conflict therewith.
>
> …
>
> (S)uch city or town, and the citizens thereof, shall have the powers set out in sections 1, 4 and 5 of this article, and all other powers necessary, requisite or proper for the government and administration of its local and municipal matters, including power to legislate upon, provide, regulate, conduct and control:
>
> …
>
> e. The issuance, refunding and liquidation of all kinds of municipal obligations, including bonds and other obligations of park, water and local improvement
>
> …
>
> g. The assessment of property in such city or town for municipal taxation and the levy and collection of taxes thereon for municipal purposes and special assessments for local improvements; such assessments, levy and collection of taxes and special assessments to be made by municipal officials or by the county or state officials as may be provided by the charter;
>
> …
>
> It is the intention of this article to grant and confirm to the people of all municipalities coming within its provisions the full right of self-government in both local and municipal matters and the enumeration herein of certain powers

> shall not be construed to deny such cities and towns, and to the people thereof, any right or power essential or proper to the full exercise of such right.
>
> The statutes of the state of Colorado, so far as applicable, shall continue to apply to such cities and towns, except insofar as superseded by the charters of such cities and towns or by ordinance passed pursuant to such charters. (emphasis added)

CO. CONST. Art. 20 Section 1 further provides that a home rule city "shall own, possess, and hold all property, real and personal," and

> "may purchase, receive, hold, and enjoy or sell and dispose of, real and personal property; may receive bequests, gifts, and donations of all kinds of property, in fee simple, or in trust for public, charitable, or other purposes; and do all things and acts necessary to carry out the purposes of such gifts, bequests, and donations, with power to manage, sell, lease, or otherwise dispose of the same in accordance with the terms of the gift, bequest, or trust; shall have the power, within or without its territorial limits, to construct, condemn and purchase, purchase, acquire, lease, add to, maintain, conduct, and operate water works, light plants, power plants, transportation systems, heating plants, and any other public utilities or works or ways local in use and extent, in whole or in part, and everything required therefore, for the use of said city and county and the inhabitants thereof, and any such systems, plants, or works or ways, or any contracts in relation or connection with either, that may exist and which said city and county may desire to purchase, in whole or in part, the same or any part thereof may be purchased by said city and county which may enforce such purchase by proceedings at law as in taking land for public use by right of eminent domain, and shall have the power to issue bonds upon the vote of the taxpaying electors, at any special or general election, in any amount necessary to carry out any of said powers or purposes, as may by the charter be provided."

Thus, under Article XX, sections 1, 4, 5, and 6 home rule municipalities have very broad authority to create or amend their charters to govern local and municipal matters, including managing money and assets. As an example, the City of Englewood, in Section 3 of its home rule charter, further provides:

> "The City shall have all powers, functions, rights, and privileges in the operation of a municipality, except those powers, functions, rights, and privileges expressly forbidden to Home Rule municipal corporations and cities by the Constitution or the Statutes of the State of Colorado."

In examining the scope of home rule authority, Colorado courts have generally upheld the rule that home rule municipalities have the authority to govern local matters. *Town of Telluride v. San Miguel Valley Corp*., 185 P.3d 161, 165 (Colo. 2008). Specific actions listed in Sections 1 through 6 of Art. XX were not intended to be an "enumeration of powers conferred, but simply the expression of a few of the more prominent powers municipal corporations are frequently granted." *Id*. Consequently, courts have concluded that the Section 6 language establishes that home rule cities have plenary power over local and municipal matters. *Id*. at 166.

While our review of municipal ordinance cases has not yielded any Colorado court decision on the establishment of a city-owned bank, the courts have generally validated a wide variety of ordinances based on the Section 6 language. Similar to *Telluride*, while the establishment of a bank is not explicitly listed as a home rule power, Section 6's "all powers" language will likely be broad enough to cover such an ordinance. In addition, we have not found any Colorado statutes expressly forbidding the creation of such bank. Accordingly, we conclude home rule cities in Colorado already have the authority to establish a city-owned bank. In *Schaefer v. City and County of Denver* the Colorado Supreme Court stated:

> The ordinance qualifies a separate and distinct group of people who are not eligible to contract a state-sanctioned marriage to receive health and dental insurance benefits from the City. Therefore, the ordinance does not adversely impact the integrity and importance of the institution of marriage.
>
> We conclude that the state has not asserted any general or particularized interest in the compensation or group health and dental benefits provided to employees of municipalities in general, and home rule cities in particular. We, therefore, conclude, consistent with Colorado Springs Fire Fighters v. Colorado Springs, supra, that the power to grant group health insurance benefits to spousal equivalents is a matter of local concern subject only to the limitations imposed by the city charter. *Schaefer v. City and County of Denver* 973 P.2d 717, 721 (Colo. 1998)

2. We have assumed for purposes of this memorandum that a public bank owned by the state or local government would be regulated by the State Division of Banking and Banking Board under applicable laws and regulations. The Colorado legislature has provided for the uniform regulation of Colorado banks. Thus, it appears probable that if a city-owned bank attempted significant variations of its operation from the provisions of state legislation that might adversely affect its financial integrity, they would likely be preempted by the state statutes governing banking in Colorado.

II. The legality and operation of public banks under Colorado statutes

A. Can a public bank obtain a charter as an LLC in Colorado?

Several statutes in Colorado establish procedures that might be used by state and local governments to create a public bank.

C.R.S. § 11-102-104 (5.5) (a) provides that a limited liability company (LLC) as defined in CRS §7-80-102 may apply for and obtain a bank charter. The definition of an LLC in CRS § 7-80-102 would not preclude a public entity from applying for and obtaining a charter.

C.R.S. §7-80-203 provides that one or more persons may form an LLC and the person need not be an individual. Therefore, an entity such a government could form an LLC and might be the only person to form the LLC.

C.R.S. § 7-80-204 (d) (III) provides that an LLC's articles of organization must provide that it has at least one member. It would be a simple matter for the state, a city, or county, to so provide in its articles of organization.

As discussed above, the Colorado constitution does not prohibit but appears to allow a home rule city to own and operate an LLC on the ground that it is "necessary" to achieve the public purposes of the government, so as to better handle its money, create a stronger, more stable economy, and generate new income without raising taxes.

Despite the foregoing analysis, we believe it would make more sense for the state to pass legislation to directly enable cities, towns, and counties, to apply for a charter to create their own public banks, rather than go through the procedure of establishing an LLC or banking corporation under existing statutes.

4. A bank must be an eligible depository under Colorado law

C.R.S. §11-10.5-106 provides that to be an eligible depository for public funds a bank must be a member of the FDIC.

C.R.S. § 11-10.5-107 A bank must have 102% collateral for its deposits

C.R.S. §24-75-603 It is lawful for cities, counties, and banks to place deposits in certain depositories, including those with 102% collateral

C.R.S. § 11-103-304 When the banking board grants a charter it shall make it contingent upon the bank applying for membership in the Federal Reserve or the F.D.I.C.

Would a chartered public bank in Colorado be required to join the Federal Reserve or FDIC?

A number of Colorado statutes bear on the above question. C.R.S. §11-10.5-104 provides that in order to hold public funds, a bank must be designated by the Colorado banking board as a public depository. C.R.S. §11-10.5-106 (2) provides that to be designated as an eligible depository the deposits of the bank must be insured or guaranteed by federal deposit insurance. C.R.S. § 11-10.5-107 (5) provides that to be an eligible depository of public funds, any such depository shall pledge collateral having a market value in excess of one hundred two percent of the aggregate uninsured public deposits. C.R.S. § 11-103-304 provides that when the banking board grants a de novo application for a banking charter, it shall make the approval contingent upon the bank making a bona fide application either to the Federal Reserve or to the Federal Deposit Insurance Corporation. C.R.S. § 24-75-603 (1) provides that it is lawful for the state or any political subdivision of the state and any bank operating under Colorado law to deposit its funds in any bank that is a member of the F.D.I.C. to the extent the deposit is insured by the F.D.I.C. or "is secured by a pledge of eligible collateral as required by statute," (i.e. 102% collateral). Finally, C.R.S. § 24-75-603 (2) provides that security for deposits of public funds shall not be required to the extent the deposits are insured by the F.D.I.C.

When reading these provisions together, it might appear that any bank, including a state or local public bank, must have federal deposit insurance, and thus be a member of the F.D.I.C. However, C.R.S. § 24-75-603 (1) provides that it would not need to be a member of the F.D.I.C. if it receives a pledge of collateral of more than 102% of its deposits. Conversely, C.R.S. § 24-75-603 (2) says it would not need to meet the 102% collateral requirement to the extent its deposits are insured by the F.D.I.C. Thus, as long as its deposits are backed by 102% collateral a bank need not join or be insured by the F.D.I.C. This interpretation is supported by the fact that C.R.S. § 11-103-304 provides that when the banking board grants a charter it shall make it contingent upon the bank either applying for membership in the Federal Reserve or in the F.D.I.C. This interpretation further makes sense because as long as a bank's deposits are fully insured or guaranteed, it should not need to have them also insured or guaranteed by another means or agency.

One practical means of providing 102% collateral for public deposits would be to request the Federal Home Loan Bank for a letter of credit for such purpose. This would require applying to the Federal Home Loan Bank in Topeka, Kansas, which serves Colorado. The letter of credit might be simpler and less costly than having the public bank supply the collateral itself.

CONCLUSION

We have shown above that the Colorado constitution, in particular, Article XI, §§ 1 and 2, under Article XI, §§3, 4, and 6, and under Article X §20 (TABOR) does not prohibit public banks, particularly when operated as TABOR enterprises or by the state or cities that have de-Bruced. Further, under the broad home rule provisions of Colorado it appears that public banks may already be legal for cities and towns, and that state legislation could authorize home rule counties to establish public banks. Further, it may be argued that the constitution Article XI, section 2 authorizes cities and towns to establish public banks in order to support the production, transmission, and distribution of energy. While it appears that the state, cities, towns, and counties might be able to establish public banks as an LLC or, less clearly, as a banking corporation, it would make sense to pass legislation to authorize cities, towns, and counties to apply for a charter directly under in their own name. It may be reasonably argued that the state and its political subdivisions have a fiduciary duty to authorize and establish public banks in order to best manage their respective assets and to avoid the substantially increased risks entailed by the current practice of placing their liquid assets in major private banks whose primary goal is to maximize their own shareholders' profits rather than the good of the community.

Respectfully submitted,

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Appendix

Public banking and public control of money have a well-established history.

Public banking and public control of money have a well-established history. Some of those who question the idea of public banks have suggested that banking is a private business and that it is not appropriate for government to be in the "business" of banking. We believe such statements violate common sense and misrepresent history, which shows that public banks in America and elsewhere have a long and honorable history.

Public banks in the world today. Today, about 25% of the world's banks are publicly owned. The countries that have public banks have had faster growing economies and stronger and more stable economies---for example Germany, Switzerland, Costa Rica, South Korea, Japan, Taiwan, and China. (Ellen Brown, *The Public Bank Solution* (2013)

America's Mostly Positive History of Public Banks and Public Currency. Our country originated from government lending and publicly issued currency, which created a high level of prosperity during the colonial era. From 1723 to 1764 the 13 American colonial governments were each able to lend money and to print their own currency, and thus establish strong economies, which Ben Franklin described as the most prosperous in the world at the time. As Franklin later wrote, when those powers were taken away by the British Parliament in 1764, over Franklin's strenuous objection, the colonies rapidly fell into widespread unemployment and poverty, which he said was the real cause of the Revolution, and not taxes such as on tea. Some of the colonies, such as Pennsylvania, managed such lending very well, while others did not manage them as well and problems developed. Proper governance and management are key essentials to successful operation of any bank.

The Continental Dollar and the American Revolution. The Continental Congress printed money in order to fund the Revolutionary War and thereby enabled the colonists to defeat the British, who at the time had the most powerful army in the world. At the end of the war, hyperinflation occurred, which was later discovered to have been caused primarily by British counterfeiting, speculating and short-selling the American "continental" dollar.

The First and Second Banks of the United States. The First Bank of the United States (1791-1811) and the Second Bank of the United States (1817-1936) were each about 80% privately owned and controlled, and only 20% owned by government, and thus cannot be truly called "public banks." The private owners included a significant proportion of foreign investors. As a result of president Andrew Jackson's vigorous opposition to the Second Bank, it was not renewed and closed in 1836.

The 19th Century Public Banks. In the first half of the 19th century, a number of states had publicly owned banks. Some were operated very successfully, but others were not well-governed. Some failed due to faulty governance and some were probably closed due to opposition from large banks. All were eventually discontinued. Some of them demonstrated that public banks can be highly successful.

The Direct Printing of Currency (Greenbacks) to Fund the Civil War. Lincoln was the only president under whom a major quantity of currency ($450 million) was issued by the U.S. Government. This was authorized by and under Article I, §8 (5) of the constitution. This action avoided the need to borrow from the New York banks, which had offered to lend to the government at 24-36% interest. The money was issued as "greenbacks" and funded 40% of the Civil War.

The Reconstruction Finance Corporation. From 1933-1945, the Reconstruction Finance Corporation functioned like a bank by lending $35 billion into the U.S. economy, which played an important role in overcoming the Great Depression and in funding World War II. It was operated without the slightest hint of scandal. It continued its operations thereafter, gradually tapering off its lending, and was unwisely closed in 1957.

The Bank of North Dakota. Finally, the success of the 100 year-old Bank of North Dakota, described above, is a further example of a highly successful and honorably managed public bank that has accomplished a great deal of good for the citizens of North Dakota.

Bank2 – the Second Public Bank in the United States. Bank2, founded in Oklahoma City in 2002, is a public bank owned by the Chickasaw Indian Nation. It has grown from $7.5 million in assets at its startup to $135 million in assets today. It has often been rated a 4-Star Bank by Bauer Financial, and was rated in the top 15% of all banks in the U.S. for 2016 by Seifried & Brew LLC. Bank2 was also recognized by the ABA Banking Journal as the #1 and #3 community bank in the nation in 2009 and 2010 respectively. https://bank2.bank/who-we-are

The Major Banks Have Performed Far Worse than Public Banks. These many current and past examples of public banks, of which we could readily supply more, show that the attempt of opponents of public banks to claim that they "won't work", or are "risky", or cannot be competently managed, is without foundation and solidly refuted by the facts. Furthermore, the main opponents of public banks represent major banks that engaged in risky investments, mismanagement, fraudulent transactions and investments resulting in several hundred $ billion in fines, and whose irresponsible conduct collapsed our economy in the 2008 Great Recession. They also have caused the failure of many private community banks which they then bought up for pennies on the dollar. Then they demanded and received massive bailouts at taxpayers' expense, and rewarded their managers for their irresponsible behavior with golden parachutes.

Since the 2008 crash the largest U.S. banks have received some $16 trillion in "quantitative easing", designed to encourage them to lend into the economy to restore it, but they instead spent the money on themselves to take their bad investments off their books. Finally, their behavior is again creating a bubble economy that may collapse, and they are pushing to roll back the very legislation enacted in the wake of the 2008 crash that was designed to reduce the chances of another such crash. These banks' warnings about public banks should be taken with a grain of salt.

Money is a public utility. Money ought to be considered a utility, like water, energy, or transportation, because everyone needs it to survive and thrive. Therefore, as Aristotle and Ben Franklin contended, and as Article I, §8 of the U.S. Constitution authorizes, money should be subject to public management. In that way, it can be harnessed to create strong and stable economies, rather than turned entirely over to private banks to maximize their own profit, which all too often works to the detriment of the public interest, as we saw with the Great Recession.

Banks create new money. Banks actually create new money when they make loans, money that did not exist before. (Bank of England, *Quarterly Bulletin,* Q1, 2014). When our state, cities, and counties put all our money as deposits in privately owned banks, then those banks create all of the money and collect all of the interest on our money, money that ought to belong to all of us, the citizens, and that should be loaned and used in our own communities, and not elsewhere solely for private bankers' profit while placing our economy at risk.