STATE OF KANSAS

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ATTORNEY GENERAL OPINION NO. 76- 108

The Honorable Fred W. Rosenau
State Representative
3rd Floor - State Capitol Building
Topeka, Kansas 66612

Re: Taxation--Tax Increment Financing--House Bill 2666

Synopsis: Section 9 of 1976 House Bill 2666 authorizes an unconstitutional diversion of ad valorem taxes levied by affected political subdivisions on taxable tangible real property located in any redevelopment area, in violation of Article 11, § 5 of the Kansas Constitution, by diverting the proceeds of levies made by affected political subdivisions for city, school and county purposes to payment of principal of and interest on special obligation bonds issued by the city to finance redevelopment projects undertaken pursuant to the act.

* * *

Dear Representative Rosenau:

You inquire concerning House Bill No. 2666, providing for the redevelopment of "downtown areas of cities" and the financing of such projects. The bill authorizes a city to acquire blighted downtown property, although no uptown or midtown property. For that purpose, and to finance any redevelopment project undertaken pursuant to the bill, the city may issue special obligation bonds which are payable, both as to principal and interest, from several sources, including "property tax increments allocated to, and paid into a special fund of the city under section 6" of the act.

Section 6 applies only to "real property taxes," defined as "all taxes levied on an ad valorem basis upon land and improvements

thereon," levied by three political subdivisions, the county, the city, and the unified school district. Subsection (b) directs that all tangible taxable property in the redevelopment project area shall be assessed and taxed as all other property:

> "All tangible taxable property located within a redevelopment project shall be assessed and taxed for ad valorem tax purposes pursuant to law in the same manner that such property would be assessed and taxed if located outside such area, and all ad valorem taxes levied on such property shall be paid to and collected by the county treasurer in the same manner as other taxes are paid and collected."

However, the distribution of the proceeds of the taxes thus levied and collected is governed by section 6(c)(1) and (2). The first subsection directs thus:

> "From the taxes levied each year by or for each of the taxing subdivisions, the county treasurer shall first allocate and pay to each such taxing subdivision all of the real property taxes collected which are produced from that portion of the assessed valuation of such real property which does not exceed that shown on the assessment roll last equalized prior to the effective date of such ordinance."

However, the increment in real property taxes levied by the city, county and unified school district in excess of the foregoing is to be applied to payment of the special obligation bonds issued by the city, under section 6(c)(2):

> "Any real property taxes produced from that portion of the assessed valuation of real property within the redevelopment project area in excess of that shown on the assessment roll last equalized prior to the effective date of such ordinance shall be allocated and paid by the county treasurer to a special fund of the city to pay the principal of and interest on any special obligation bonds issued by such city to finance, in whole or in part, such redevelopment project. When such special

> obligation bonds and interest thereon have been paid, all moneys thereafter received from real property taxes upon the taxable tangible property within such redevelopment project area shall be allocated and paid to the respective taxing subdivisions in the same manner as are other ad valorem taxes."

The question which is raised is whether the use of the proceeds from real property taxes levied by the city, county and unified school district derived from that portion of the assessed valuation of the redevelopment area which is in excess of that shown on the assessment rolls last equalized prior to the effective date of the ordinance for deposit in a special fund of the city to pay principal and interest on special obligation bonds of the city issued under this bill, and not for the purposes of the unified school district or the county, *e.g.*, for which they were levied, violates Article 11, section 5 of the Kansas Constitution, which states thus:

> "No tax shall be levied except in pursuance of a law, which shall distinctly state the object of the same; to which object only such tax shall be applied."

In Opinion No. 74-207 addressed to Senator Elwaine Pomeroy, Attorney General Vern Miller pointed out that 1974 House Bill No. 1745, the predecessor of this bill, was defective on this score, stating thus:

> "Under § 2(b), that portion of ad valorem taxes collected in excess of the amount distributable to the taxing subdivisions in behalf of which they were levied and collected under § 2(b) is not be paid to and used by those taxing subdivisions, but, on the contrary, is to be paid to the urban renewal agency for deposit in a 'special fund' for the financing and repayment of the indebtedness of the urban renewal agency. Article 11, § 5 is unambiguous and forthright. The proceeds of an ad valorem may be applied only to the 'object' for which the tax is authorized by law to be levied. Any use of funds derived from levies imposed by the local taxing subdivisions for any purposes other than stated in the statutes authorizing such levies would plainly violate this provision.

> To devote any portion of the proceeds of a levy imposed for, e.g., a board of education, to the financing of the indebtedness of an urban renewal agency would be in direct violation of Article 11, § 5 of the Kansas Constitution."

Section 9 of the present bill was drawn in an effort to forestall this objection. It states thus:

> "Notwithstanding any other provision of law, it is hereby stated that it is an object of all ad valorem taxes levied by or for the benefit of any city, county or school district of the state on taxable tangible real property located within any downtown redevelopment project undertaken pursuant to this act, that such taxes may be applied and allocated to and when collected paid into a special fund of a city pursuant to the procedures and limitations of this act to pay the principal of and interest on special obligation bonds issued by such city to finance, in whole or in part, such redevelopment project."

Section 9, unfortunately, is but a cosmetic effort to disguise a flagrant disregard of Article 11, § 5. The Kansas Supreme Court has long held that this section means precisely what it says. Precedent on this question is nearly a century old. In *A.T. & S.F. Railroad Co. v. Woodcock*, 18 Kan. 20 (1877), Sedgwick County levied the maximum tax permitted by law, one percent on the value of the taxable property of the county, and in addition levied a tax of eight mills to meet a deficit in county revenue in the preceding year, with no apparent authority therefor. The Legislature passed a purported curative act, stating that "all levies of taxes heretofore made by the board of county commissioners of Sedgwick County, Kansas, in the year 1974, be and the same are hereby legalized." The validity of the right mill tax was subsequently challenged, and the court held it to be without authority:

> "But was said tax made valid by the subsequent passage of said act of the legislature? We think not. And two reasons may be offered therefor: 1st, The tax was void

> when levied, not because of any mere irregularity in the tax proceedings, but because the commissioners had no power to levy the same. 2d, the only act or law upon which the supposed validity of said tax is founded, (the curative act of 1875, above quoted,) does not in any manner state the object of the tax."

Referring to the constitutional provision, then Article 11, § 4, the court stated thus:

> "Now the tax in question in this case was not only not *levied* 'in pursuance of a law,' but it is not *sustained* by any law which "distinctly states the object of the same.' This we think is fatal to the tax. It is possible however that it is not necessary that the curative act should in all cases state the object of the tax. When a tax is levied in pursuance of a law, and that law itself distinctly states the object of the tax levied under it, it would seem that that should be sufficient. If for some defect or irregularity in the tax proceedings it were thought that the tax were illegal and void, or voidable, and therefore a curative act should be passed for the purpose of validating such tax, it would probably not be necessary in such a case that the curative act should also distinctly state the object of the tax. But still, it is probably necessary in all cases that every tax should be sustained by some law which should distinctly state the object of such tax." [Emphasis by the court.]

In *National Bank of Lawrence v. Barber*, 24 Kan. 534 (1880), the court considered a statute which authorized any township which had subscribed to the stock of a railroad which had constructed all or any part of its line in said township, to retain all county and township taxes levied on said railroad property, to be applied to payment of principal and interest on said bonds. A holder of railroad bonds sued the county treasurer to recover a portion of the sum so collected and set apart for the township for railroad bond purposes. The court held that the statute sought to effect an unlawful diversion of tax revenues from the purpose for which they were levied:

"This county tax, which is now in litigation, is a portion of the general county tax which was levied on all the taxable property of the county by the county commissioners for general county purposes . . . . This general county tax was levied for 'county purposes,' for 'county charges and expenses,' for 'current expenses of the county,' and no portion of it was levied for the purpose of paying principal or interest on township railroad bonds. And it was levied for said 'county purposes' 'in pursuance of a law;' and therefore, no portion of it can now be diverted from such purpose or purposes. . . . Certainly no portion of this tax was levied for the purpose for which the plaintiff now desires to use it.

The tax now in litigation either is or is not a part of the county tax. If it is, then it cannot be diverted from county purposes as before stated. But if it is not, then neither it nor the real county tax is levied on the taxable property of the county or township at 'a uniform and equal rate.' That is, if it is not a part of the county tax, then all taxable property in the county, except the railroad property, in which this tax was levied, is subject to a county tax, while this railroad property is not subject to any county tax, and no property in the county or township, other than this railroad property, is subject to so high a township railroad bond tax, as this railroad property is . . . . Hence, it will be seen that if the tax now in litigation is not a county tax or a part thereof, then neither it nor the real county tax is levied on the taxable property of the county and township at 'a uniform and equal rate,' and hence both it and the statute attempting to create it must be held to be void. Besides, if it is not a county tax, then both it and the statute attempting to create it, must be held to be void, for the additional reason that it is not levied in pursuance of any law which distinctly states the object of the tax. . . . No statute can be found authorizing the levy of any such tax. And it will not do to call it a county tax for the purpose of giving authority to the county commissioners to levy it under the statutes which authorize the levy of county taxes, and also for the purpose of avoiding that constitutional provision which requires the tax to be imposed at a uniform and equal rate, and then, after the tax

> is supposed to be legally levied, to say that it is not a county tax for the purpose of avoiding that other constitutional provision which requires that a tax shall be applied only to the object for which it was levied. It either must or must not be a county tax, and in either case the statute attempting to apply it as a township railroad bond fund must be void."

The court pointed out that because the proceeds of the county tax upon the railroad property are held by the county treasurer for the benefit of the township to be applied to the payment of interest and principal of railroad bonds to which the township has subscribed, the railroad company is exempted from bearing its just proportion, or indeed any proportion, of the expenses or other indebtedness of the county or township. In short, the court found it be a "clear attempt on the part of the statute to divert funds, raised by taxation for one object, to another object."

In *State ex rel. Smith v. Board of County Commissioners of Saline County*, 128 Kan. 437, 278 Pac. 54 (1929), the court held invalid a statute authorizing counties to advance to the State Highway Commission monies to finance the construction or reconstruction or sections of the state highway system in such counties. Saline County commissioners passed a resolution agreeing to advance the sum of $210,000 to finance highway improvements in that county, to be derived from the county road fund, the county bridge fund, the county general fund, the sinking fund, the bond fund, the twenty per cent state road fund, and from deficiency warrants issued against each of these funds. The court stated thus:

> "It may be conceded that there is authority in the legislature to control the finances not only of the state but also of its municipalities, and to provide for the transfer of funds from one to the other unless prohibited by constitutional limitations. There is a limitation that 'No tax shall be levied except in pursuance of a law which shall distinctly state the object of the same, to which object only such tax shall be applied.' . . . This restriction is an insuperable barrier to the loaning of the funds named or to their application to the building of state highways. The taxes were levied in pursuance of law for specific purposes, and the funds derived from

> these levies must be exclusively applied to those purposes. Each of the funds is distinct from the others and it is beyond the power of the commissioners or others to divert funds raised by taxation for one purpose and apply them to another." 128 Kan. at 439-440.

See also State ex rel. Board of County Commissioners v. Crawford Township, 135 Kan. 553, 32 P.2d 809 (1934).

No section of 1976 House Bill No. 2666, including section 9, purports to authorize the levy of any tax whatever. That section does, however, purport to divert proceeds of every ad valorem tax acknowledged and stated to be "levied by and for the benefit of any city, county or school district of this state" on property located in a redevelopment project undertaken pursuant to the bill, from the political subdivisions which levied the taxes, and authorizes the application of those funds to payment of principal of and interest on special obligation bonds issued by the city to finance the redevelopment project.

The levy of taxes is an exercise of legislative power. Article 11, § 5 requires that every tax be levied pursuant to a law, which shall state the object of that tax. With the adoption of Article 12, § 5, Kansas cities enjoy a direct constitutional grant of legislative power to "determine their local affairs and government, including the levying of taxes . . . ." Article 12, § 5(b). Article 11, § 5 applies to taxes levied pursuant to municipal legislative authority. *State of Kansas ex rel. v. City of Emporia*, 57 Kan. 710 (1897). Thus, a municipal tax levied pursuant to a city ordinance, whether a charter ordinance or a regular ordinance, must be devoted to the purpose stated in that ordinance. A subsequent diversion of the proceeds of that tax to another purpose is prohibited.

To cite but one example, K.S.A. 12-1617h authorizes incorporated cities to make a levy on all taxable tangible property within the city for the purpose of creating a fund to be used in securing industries or manufacturing institutions for such city or near its environs. The statute meets the constitutional requirement, in that it both authorizes a levy and states the object thereof. No such levy may be made until approved by a "majority of all the votes cast on this proposition at an election." The purpose for which the levy is to be made and its proceeds expended is thus fixed by the statute and by the proposition approved by the voters. Article 11, § 5 forbids the exercise of any legislative power, whether by the city governing body or the state legislature, to divert the proceeds of that levy to any other purpose. Section 9

of House Bill 2666 does not, of course, amend K.S.A. 12-1671h, or the proposition which may have been approved by the voters. Notwithstanding, it would permit the diversion of the proceeds of that levy, as well as every other levy of the city upon taxable tangible real property, for a purpose entirely foreign to the purpose for which the levy was authorized, the payment of principal of and interest on special obligation bonds issued to finance a redevelopment project. Likewise, a recreation levy under K.S.A. 12-1901 *et seq.* would be similarly diverted as would a host of other levies of the affected political subdivisions. Section 9 is artfully worded to allege formal compliance with Article 11, § 5. The sweeping legislative declaration that "it is an object of all ad valorem taxes levied by or for the benefit of" any affected political subdivision to "pay the principal of and interest on special obligation bonds issued by such city to finance, in whole or in part, such redevelopment project." This does not satisfy Article 11, § 5, which requires that any tax which is levied shall be "in pursuance of a law," *i.e.*, authorized by legislative act, which legislative act shall "distinctly state the object of the same," and "to which object only such tax shall be applied." Section 9 of House Bill 2666 does not authorize any levy whatever for any political subdivision. No legislative body, whether it be the state legislature, a city governing body, or a board of county commissioners, may by legislative act authorize the expenditure of the proceeds of a tax for any purpose other than that stated in the law, ordinance or resolution which authorizes the tax, except as authorized by K.S.A 79-2958.

A member of my staff appeared before an interim legislative committee in the summer of 1975, to point out this problem, and urged that attention be given to a comprehensive amendment of the various affected levy statutes. For whatever reason, this advice was disregarded, and section 9 was settled upon as a kind of token compliance with Article 11, § 5. In my opinion, it is a transparent subterfuge, which complies neither formally nor substantively with the requirements of that section.

Accordingly, it is my opinion that section 9 of House Bill 2666 authorizes a use of the ad valorem tax levies of the affected political subdivisions for a purpose, the payment of principal of and interest on special obligation bonds issued under the act, other than stated in the statutes, ordinances and resolutions authorizing levies of those political subdivisions, and is thus in violation of Article 11, § 5 of the Kansas Constitution. It is unnecessary to reach the question whether the bill results in unequal assessment and taxation

raised in *National Bank of Lawrence v. Barber*, 24 Kan. 534 (1880), discussed above.

Yours very truly,

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CURT T. SCHNEIDER
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