



STATE OF KANSAS

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Curt T. Schneider  
Attorney General

February 7, 1978

ATTORNEY GENERAL OPINION NO. 78-65

Mr. John Dekker  
Director of Law  
City Hall - Thirteenth Floor  
455 North Main Street  
Wichita, Kansas 67202

Re: Cities--Funds--Disposition

Synopsis: Moneys received from Blue Cross-Blue Shield as divisible surplus under a group hospitalization insurance contract held by the City of Wichita for the benefit of its participating employees should be distributed to the city and its employees on the basis of their respective contributions to the premium costs of the policy. The city having contributed three fourths of the premium costs, it is entitled to three fourths of the total amount of said divisible surplus. Because the participating employees contributed one fourth of the total subscription costs under said policy, those employees are entitled to share in one fourth of said sum. The portion allocated to the city is properly credited to the city general fund. The budget of the city may be amended to provide budget authority for the expenditure of said money, provided notice and opportunity for a public hearing on said proposed amendment are furnished to the public as required by the Kansas budget law, K.S.A. 79-2925. The interest earned on said monies while held awaiting final disposition thereof should be distributed in the same manner as the principal, one fourth to participating employees and three fourths to the city.

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Dear Mr. Dekker:

On behalf of the City Commission of the City of Wichita, you request my opinion concerning the legality of the disposition of a portion of certain monies which have been received by the City of Wichita from the Kansas Blue Cross, pursuant to a group health insurance contract purchased by the City of Wichita for its employees.

You advise that in 1969, on behalf of its employees, the city negotiated with Blue Cross to establish a group coverage contract providing hospital insurance for the city employees. Under date of September 1, 1969, Blue Cross issued a group contract to the "City of Wichita Employees," designated as holder of the contract, a copy of which you enclose with your letter.

Subsequent to September 1, 1969, the city has annually budgeted to pay a portion of its employees' Blue Cross subscription costs, the employees paying that portion of the subscription not borne by the city. For the past several years, and during the contract year from September 1, 1977, through August 31, 1978, the city has paid seventy-five percent (75%) and each participating employee has paid twenty-five percent (25%) of the cost of each participating employee's Blue Cross insurance coverage.

During the period of time in question herein, the city had two classes of employees, those represented by labor organizations, and those represented by an employee council. All labor organizations representing city employees have negotiated and entered into contracts with the city, which set out the terms of the employment contract. The employees council does not negotiate labor contracts for the employees it represents, and employment benefits for those employees are determined as a matter of city policy, pursuant to funding approved by the city commission in the adoption of the city budget. Under the city's policy and the union contracts, each employee is free to elect to participate or not to participate in the group insurance plan.

On December 28, 1977, the city received a check from Blue Cross, payable to the Wichita City Employees as holder of the contract, in the amount of \$543,407.74. The check represents what is designated as divisible surplus under article X of the group insurance contract. "Divisible surplus" represents that portion of the income which is derived only from subscription charges for the Contract and "is available for a retroactive adjustment of subscription charges." Subscription charges are the payments made by a subscriber to acquire coverage under the group contract, and in this instance includes all city employees who have elected to participate in the group contract. Thus, "divisible surplus" represents the difference between premium charges assessed by Blue Cross as based upon estimated costs, and the premiums necessary to provide the insurance protection and reserve based upon actual costs during the term of the contract year.

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During the year for which Blue Cross has refunded the "divisible surplus" in question, the city has paid over to Blue Cross in premiums on behalf of its employees the sum of \$3,364,322.62, of which the employees contributed \$841,080.67 and the city paid \$2,523,241.05. These payments are in accord with both the city's policy regarding its unrepresented employees and its contractual obligations to its organized employee groups.

Now, the question has arisen as to the disposition of the amount in question. There appears to be complete agreement that 25% of the divisible surplus should properly be distributed among the city employees who participated in the insurance plan as subscribers, that representing the proportion of the total premium derived from employee contributions. There is no agreement whatever regarding disposition of the remaining 75%.

Counsel for the Fraternal Order of Police, Lodge No. 5, Service Employees Union Local 513, the Firefighters Local 666, and the Employees Counsel has furnished us with a statement of the position of the employees. Their claim to the balance of the divisible surplus is twofold. First, a claim is asserted on the basis of the insurance contract itself. Article X, paragraph C states thus:

"Divisible surplus is distributed in this manner:

1. To meet the Contract Holder's minimum group reserve needs, if any, under his Kansas Blue Shield Group Contract;
2. The remainder, if any, is paid in cash to the Contract Holder or upon written request applied as an adjustment of future subscription charges."

Paragraph D states, further:

"Any portion of the divisible surplus that is paid in cash and that is in excess of the Contract Holder's share of the subscription charges shall be applied for the sole benefit of the enrolled Subscribers."

Counsel notes that the contract recites on page A-1 that the group contract is issued to "City of Wichita Employees," as "Contract

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Holder." The check made out in payment of the divisible surplus was made out to the "City of Wichita Employees." Counsel for the employees accordingly argues that the employees are themselves the holder of the contract, but that the group contract runs between Blue Cross-Blue Shield and the employees, and the city is not a party to the insurance contract. Thus, it is urged, the city has "absolutely no legal claim upon this money," and may only distribute it to the participating employees on a prorated basis.

In my judgment, this contractual claim is specious. Clearly, the city is the holder of the contract, and its employees who participate in the hospitalization insurance plan are subscribers. Article I, paragraph B defines the latter term thus:

"Subscriber means any employee or member of the Contract Holder who enrolls under this Contract as provided in Article II; and under a family membership also means the Subscriber's spouse and each unmarried dependent child by birth or adoption under 21 years of age."

Article IV, as well as other provisions of the contract, make a clear and obvious distinction between the terms "contract holder" and "subscriber." Since 1968, the city has acted as contract holder, in performing the duties and obligations of that party to the contract in remitting subscription charges, furnishing information to the insurer for the purpose of enrolling and terminating individual subscribers, and bearing its own share of the subscription costs as provided in its memoranda of agreement with its own employees. The contract clearly misidentifies the employees themselves as the contract holder, whereas the city is in fact the holder of the contract. Article IX, paragraphs C and D, contemplate that the divisible surplus may be allocated by the contract holder to and for the benefit of its enrolled subscribers. Once the necessary portion thereof is set aside for the contract holder's minimum group reserve needs, the remainder is paid to the "contract holder," which, in my judgment, is the City of Wichita. Any portion of that amount which is paid in cash to the contract holder which "is in excess of the Contract Holder's share of the subscription charges" shall be applied for the sole benefit of the enrolled Subscribers." Clearly, then, the employees' claim to the divisible surplus is based on the proportion of its contributions to the subscription charges.

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The employee contributions totalled 25% of the total charges, and the city's contributions totalled 75% of those charges. The city, thus, is entitled under the contract to 75% of the divisible surplus, and the employees are entitled to 25%.

The employees' claim to the entire amount of the divisible surplus is also asserted on an alternative ground, which in my judgment is equally baseless. During the meet and confer sessions leading to execution of memoranda of agreement concerning conditions of employment, pursuant to K.S.A. 75-4321 *et seq.*, it is asserted, the city represented that it had a certain dollar amount available for salaries and benefits. On the basis of that representation, agreements were reached for the city to contribute 75% of the cost of the subscription charges under the group hospitalization contract. Presumably, if the employees had elected to receive their benefits entirely in salary and without any provision for employer contribution to the contract subscription charges, the entire sum would have been available for distribution among the employees in the form of salary. Apparently, it is urged that because of a return to the city of a portion of the divisible surplus on the basis of its contributions to the insurance subscription charges, it is suggested that the memoranda of agreement obligate the city to pay over to the employees its share of this return. We have reviewed executed memoranda of agreement between the employee organizations and the city. For example, Article 11 of the memorandum of agreement with Local 666, International Association of Firefighters, provides only thus respecting the hospitalization insurance:

"Policy currently in effect covering Hospitalization shall continue. The city shall contribute 75% of the total cost, and the employee shall contribute 25%. The Hospitalization insurance program is optional."

Paragraph 12.00 of the memorandum of agreement with the Service Employees Union Local 513, AFL-CIO, CLC, provides only that the "city shall continue the present insurance plan (Blue Cross/Blue Shield Plan) now in effect." The memorandum of agreement with the Fraternal Order of Police, Lodge No. 5, provides thus:

"The City agrees to provide the same medical and hospitalization insurance coverage as provided to all other fulltime City employees."

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The City shall continue to contribute 75 percent of the total cost, and the employee shall contribute 25 percent. Said insurance coverage shall remain the same as provided in current practice or the equivalent thereto. This insurance program is optional with each employee. The bargaining unit employees agree to be bound by any changes in this insurance coverage that are approved by a majority vote of all employees covered thereunder."

There is no obligation under any of the memoranda of agreement whereby the City is required to distribute to the subscriber-employees any portion of the divisible surplus in excess of the proportion thereof represented by employee contributions. Assuming the correctness of the employee representatives' contentions, that during negotiation of the memoranda of agreement the city did in fact represent that it had available a fixed amount, approximately \$2.5 million, either for its contribution to a group hospitalization insurance contract premium or for direct allocation to salary, the employee representatives obviously either chose or accepted the former alternative, and the city did in fact pay the amount as it had agreed to do. In my judgment, the city is under no legal or contractual obligation to allocate the 75% share of the divisible surplus among its employees who elected to participate in the policy.

Concluding as I must, that 75% of the divisible surplus belongs to the City, the question remains what disposition the city is legally free to make of the money. As money paid to the city to which it is legally entitled, the city's share of the divisible surplus should be credited to the city general fund. It is permissible that the money be returned to the funds of origin, but, assuming the employer contributions are drawn from the budgets of the respective city agencies and departments, a substantial bookkeeping task would result from any effort to allocate the city's share of the divisible surplus directly back to each fund of origin. Any portion of the returned divisible surplus which is attributable to any city utility and derived from an enterprise fund, however, should be returned to that fund, rather than deposited in the city general fund.

Concluding, as I must, that 75% of the divisible surplus properly belongs to the City of Wichita, the question remains which of

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several alternative dispositions of the money are available to the city. You pose several alternatives, including return of the sum to the participating employees in a single lump sum on a pro rata basis, deposit in an escrow account to be applied to offset future increases in employee rates or in both employee and city rates, or distribution among employees based "upon a determination as to the extent of the effect of the employees' actions upon the refund." The monies involved constitute public funds, and the city governing body is free to make any disposition of the money which it deems to serve a public purpose. It may not, of course, make gifts of the money to its employees as private parties for their personal gain. However, if the governing body were to determine, for example, that pro rata rebates or refunds of some or all of the money to its participating employees as an incentive for continued lowered utilization of the group hospitalization policy to reduce future rate increases payable by the city, were in the corporate interests of the city, it is certainly free to do so. Alternatively, the governing body is free to apply the monies to offset future increases in the costs of the group hospitalization plan or, indeed, deposit the money in the city general fund to defray any other expenditures of the city.

If, as suggested, the city's portion of the surplus is deposited in the general fund, you indicate some concern that the expenditure of this money was not budgeted for the current fiscal year. In Opinion No. 74-244, dated July 29, 1974, the Attorney General advised that the Office of Revenue Sharing of the U.S. Department of the Treasury had required that revenue-sharing monies be budgeted in the same fashion as local funds, and withdrew a previous opinion to the contrary. As a result of the July 29, 1974, opinion, many taxing subdivisions were constrained to amend budgets which were already adopted or were in the process of adoption. Thus, adoption of many budgets would be completed other than in strict compliance with the schedule therefor prescribed by the budget law, K.S.A. 79-2925 et seq. The Attorney General concluded, however, that the statutory dates for adoption of the budget were directory and not mandatory, however, and accordingly, a budget could be amended even if that delayed final adoption past the statutory date set therefor. In *School District No. 40 v. Clark County Commissioners*, 155 Kan. 636, 127 P.2d 418 (1942), the court stated thus:

"There is a rule of statutory construction familiar to all lawyers, which is that when

the legislature prescribes the time when an official act is to be performed, the broad legislative purpose is to be considered by the courts whenever they are called upon to decide whether the time prescribed by statute is mandatory or directory. If mandatory, there must be strict conformity. If directory, the legislative intention is to be complied with a [sic] nearly as practicable. Instances of the latter sort frequently arise, and indeed they are particularly applicable in respect to the official mode of procedure in matters of taxation. For example, it is the duty of the board of county commissioners at its meeting on the first Monday in August to order the proper levies of every sort to be extended on the tax rolls. . . . Instances are not rare where the board has declined or failed to make a particular levy; mandamus is invoked and a decision must be reached some weeks later holding that the contested levy should be made, and it is then made, although the directory time at which it should have been made has passed. Again, the statute says the county clerk shall prepare and deliver the tax rolls to the county treasurer on or before November 1. . . . If the work of preparing the tax rolls is not completed by the statutory date (and litigation over the legality of levies or other untoward circumstance sometimes causes delay), the statutory date on which the tax rolls should be delivered to the county treasurer must of necessity be regarded as directory rather than mandatory. Although the tax rolls are not delivered to the treasurer by the time directed by the statute, nevertheless we all have to pay our taxes when the belated delivery is made! . . . ." 155 Kan. at 638-639.

In *City of Hutchinson v. Ryan*, 154 Kan. 751, 121 P.2d 179 (1942), the court quoted from 59 C.J. 1078 thus:

"'A statute specifying a time within which a public officer is to perform an official act regarding the rights and duties of



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others, and made with a view to the proper, orderly, and prompt conduct of business is usually directory, unless the phraseology of the statute, or the nature of the act to be performed and the consequences of doing or failing to do it at such time, is such that the designation of time must be considered a limitation on the power of the officer. So a statute requiring a public body, merely for the orderly transaction of business, to fix the time for the performance of certain acts which may as effectually be done at any other time is usually regarded as directory . . . ." 154 Kan. at 757.

The budget law, K.S.A. 79-2925 *et seq.*, prescribes the procedure for the adoption of municipal budgets and certification thereof for the levy of taxes. The governing body is required to prepare a budget by August 1 of each year, K.S.A. 79-2927, hold a public hearing thereon with at least 10 days published notice thereof and at least 10 days prior to certification of levies to the county clerk, K.S.A. 79-2929 and -2933, and certify the duly adopted budget to the county clerk by August 25. These dates are prescribed in order to assure the orderly computation and levy of taxes based upon the budgets so adopted. When the budget is proposed to be amended in order to provide for the expenditure of revenues which are not derived from ad valorem property taxes, such as those involved here, which derive, indeed, entirely from a non-tax source, I see no reason why the budget law should be construed to prohibit the adoption of such amendments at any time during the fiscal year, so long as the procedures are followed which are provided for the protection of the taxpayer, *i.e.*, published notice of and opportunity for participation in a public hearing upon such proposed amendments. Those dates prescribed by the budget law are obviously set out not for the protection of the public, but for the orderly and timely adoption of budgets upon which tax levies may be determined and extended. Amendment of a budget in order to provide for the expenditure of revenues derived from a source other than taxes which are levied on November 1 of each year can, consistent with this procedure, be performed as well in January as in August of any year, because the additional revenues are derived independently from property tax sources, and entail no duty on the part of the county clerk in the levy of taxes on November 1. Those features of the budget law which

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are provided for the protection of the public, *i.e.*, at least ten days' published notice of and a public hearing upon the adoption of a budget or amendments thereto, may be observed as well at any time of the year as at an August hearing.

Although the budget law makes no express provision for amendments of the budget during the fiscal year, its time constraints are clearly directory, and do not prohibit the amendment of a budget at any time during the year when the city receives additional revenues from a non-property tax source and which are available for expenditure provided there is budget authority therefor. Any such amendment procedure must include, of course, published notice thereof and a public hearing upon such proposed amendments, providing to the public opportunity for participation equal to that afforded at the annual budget hearing in July or August of each year. To conclude otherwise would result in the paradoxical situation in which a city, *e.g.*, which had sufficient unanticipated non-tax revenue to meet unforeseen expenditures would nonetheless be compelled to apply to the board of tax appeals for authority to borrow money through the issuance of no-fund warrants, thereby incurring substantial expense to borrow funds to pay bills for which the city already has sufficient revenue and which it is unable to spend merely because it lacks budget authority therefor.

The overriding purposes of the budget law are, first, to provide an orderly and timely method for the preparation and adoption of budgets and certification thereof for the levy of taxes, and to provide for public participation in the budget adoption process. Where the adoption of a budget provides only for the expenditure of previously budgeted revenues available from non-property tax sources, the first consideration is simply irrelevant. The second concern, that of public participation, may be served equally by notice and opportunity for hearing provided for amendment of the budget at any time during the fiscal year when and as the needs of the city call for the expenditure of non-property tax revenues the receipt of which was not anticipated in the budget as certified in August of the preceding year.

Accordingly, it is my opinion that the city may amend its current budget to provide for the expenditure of the moneys in question.

Lastly, you request my opinion concerning the disposition of interest earned on the divisible surplus while they are being held pending final disposition of the moneys. Interest which is attributable to one fourth of the money should be allocated for distribution among the participating employees who are eligible for

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distribution of one fourth of the divisible surplus itself. The balance of the interest should be credited to the city general fund.

Yours truly,



CURT T. SCHNEIDER  
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