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ATTORNEY GENERAL OPINION NO. 83- 31

The Honorable Ed C. Rolfs
State Representative, Sixty-Fifth District
Room 155-E, Statehouse
Topeka, Kansas 66612

Re: Roads and Bridges -- Express Highways and Freeways --
Debt Service Requirements on Highway Bonds

Taxation -- Motor-Fuel Taxes -- State Freeway Fund

Synopsis: The legislature may not enact a law which impairs the state's obligation to make the required principal and interest payments on the issued and outstanding highway bonds providing funds for the construction, reconstruction and improvement of highway projects within the state system of modern express highways and freeways. Said bonds are payable solely from the state freeway fund, and the required principal and interest payments constitute a first lien and claim on moneys accruing to said fund. Thus, even though the legislature may lawfully transfer moneys from the freeway fund to the highway fund, any law providing for such a transfer that impairs the state's contractual obligation to make the required principal and interest payments is invalid. Cited herein: K.S.A. 68-2094, 68-2096, 68-2301, 68-2302, K.S.A. 1982 Supp. 68-2304, K.S.A. 68-2305, 68-2306, 68-2308, 68-2312, K.S.A. 1982 Supp. 79-3401, 79-3425, K.S.A. 79-3474, 79-3490, K.S.A. 1982 Supp. 79-34,104.

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Dear Representative Rolfs:

You have posed several questions regarding Governor Carlin's proposal that the 1983 Legislature authorize certain transfers of moneys from the state freeway fund to the state highway fund over the next several fiscal years. Before addressing

your specific questions, it is appropriate to note that the state freeway fund is created by K.S.A. 1982 Supp. 79-3425. It was created in 1969 (L. 1969, ch. 462, §3), in conjunction with the establishment of a state system of modern express highways and freeways (K.S.A. 68-2301), and as originally enacted, all moneys deposited in the fund were to be "expended by the state highway commission for the construction of the state system of express highways and freeways." L. 1969, ch. 462, §18(b).

At the time the fund was created, specified portions of the taxes imposed under the Motor-Fuel Tax Law (K.S.A. 79-3401 et seq.) and the Special Fuels Tax Law (K.S.A. 79-3474 et seq.) were the sources of revenues deposited in the fund. In 1970, K.S.A. 79-34,104 was amended to also require a portion of the taxes collected under the Liquefied Petroleum Motor Fuel Tax Law (K.S.A. 79-3490 et seq.) to be deposited in the freeway fund.

In 1972, the legislature authorized the state highway commission to "[i]ssue highway bonds of the state of Kansas, payable solely from revenues accruing to the state freeway fund and pledged to their payment, for the purpose of providing funds for the construction, reconstruction and improvement" of highway projects within the system of modern express highways and freeways. L. 1972, ch. 252, §§1, 2. Sections 1 to 11, inclusive, of that act are now codified at K.S.A. 68-2302 to 68-2312, inclusive, and amendments thereto.

K.S.A. 1982 Supp. 68-2304 provides in part: "The principal of and the interest on such bonds shall be payable solely from the state freeway fund." This language remains unchanged since the time of the section's enactment. Similarly, K.S.A. 68-2305 provides (as it did in 1972) as follows:

"Bonds issued under the provisions of this act shall not be deemed to constitute a debt of the state or of any political subdivision thereof or a pledge of the faith and credit of the state or of any such political subdivision thereof, but all such bonds shall be payable solely from revenues accruing to the state freeway fund and pledged for their payment. All such bonds shall contain on the face thereof a statement to the effect that neither the state nor the commission shall be obligated to pay the same or the interest thereon except from moneys accruing to the state freeway fund pledged to the payment of such bonds, and that the faith and credit of the state are not pledged to the payment of the principal of or the interest on such bonds."
(Emphasis added.)

Also, K.S.A. 68-2306 provides in pertinent part:

"The secretary of transportation is hereby authorized and empowered, in the manner provided by law, to withdraw in each year from the state freeway fund and the state freeway construction fund, upon duly executed order or voucher of said secretary to the state director of accounts and reports, such amount or amounts as shall be required in such year for paying the interest on all highway bonds or highway refunding bonds issued by the secretary under this act; for retiring such bonds by their maturity or maturities; for creating reserves for such purposes; for paying the premium, if any, on a specified aggregate principal amount of such bonds which would be payable in such year if such principal amount of bonds were to be redeemed prior to their maturity or maturities; for doing any of the acts authorized by K.S.A. 68-2311; and for paying any administrative or other expenses incurred in carrying out the powers granted by this act.

"The method of computing the amount or amounts which will be required in each such year to provide for paying the interest on and retiring such bonds by their maturity or maturities, creating reserves for such purposes and paying any administrative or other expenses shall be determined as provided in the resolution of the secretary authorizing the issuance of the bonds.

"The payments provided to be made in any year pursuant to the provisions of this section from the state freeway fund shall be a first lien and claim on the state freeway fund."
(Emphasis added.)

This section has remained unchanged since its enactment in the 1972 act, except for editorial changes in 1975 (L. 1975, ch. 427, §229) to accommodate the establishment of a state department of transportation to succeed the state highway commission.

In section 12 of the 1972 act, K.S.A. 1971 Supp. 68-2301 also was amended. One of these amendments changed the purposes of the state freeway fund, as stated in subsection (b) thereof, to be as follows:

"Subject to the provisions of section 10 [K.S.A. 68-2311] of this act, all of the moneys deposited in the state freeway fund . . . shall be expended by the state highway commission for the construction, reconstruction, improvement and maintenance of the state system of express highways and freeways . . . and for the retirement of highway bonds and highway refunding bonds issued under the provisions of this act." (Emphasis added.)

Subsequent to 1972, the foregoing provisions of K.S.A. 68-2301(b) have been amended from time to time (see L. 1974, ch. 226, §6, L. 1975, ch. 357, §1, L. 1975, ch. 427, §226, L. 1979, ch. 323, §8), and the corresponding provisions of this statute now state:

"All of the moneys deposited in the state freeway fund created in K.S.A. 1979 Supp. 79-3425, and any amendments thereto, except moneys accruing to said fund as a result of the interest or earnings from the investment of moneys in the state freeway fund or in the state freeway construction fund, as provided in subsection (c) of K.S.A. 68-2311, shall be subject to transfer to the state highway fund, as provided by said K.S.A. 1979 Supp. 79-3425, and amendments thereto. After any such transfer, and subject to the provisions of K.S.A. 68-2311, the moneys remaining in the state freeway fund shall be expended by the secretary of transportation for: The construction, reconstruction, improvement and maintenance of the state system of express highways and freeways established in subsection (a) of this section; for the retirement of highway bonds and highway refunding bonds issued under the provisions of this act; and for the purpose of making payments to the Kansas turnpike authority pursuant to the provisions of K.S.A. 68-2096, except that such payments shall not be made from the interest or earnings from the investment of moneys in the state freeway construction fund, as provided in K.S.A. 68-2311. Moneys in the state freeway fund may be transferred to the state highway fund and may be expended from such fund for (1) the construction of state highways within the corridors designated in subsection (a) and approved by the secretary of transportation prior to the effective date of this act; (2)

the construction of bypass routes not exceeding five (5) miles in length; and (3) the reconstruction, improvement and maintenance of state highways, whether or not such highways are within the corridors designated in subsection (a). Such reconstruction, improvement and maintenance shall be according to need as determined by priorities assigned to such state highways by the secretary of transportation in accordance with established standards and criteria." (Emphasis added.)

We also note that K.S.A. 68-2308 provides for the rights of bondholders, as follows:

"The resolution authorizing the issuance of highway bonds under the provisions of this act may provide that a specified number of holders of such bonds, or any of the coupons appertaining thereto, either at law or in equity, by suit, action, mandamus or other proceedings, may protect and enforce any and all rights under the laws of the state or granted hereunder or under the resolution or resolutions authorizing the issuance of such bonds, and may enforce and compel the performance of all duties required by this act or by such resolution to be performed by the secretary of transportation or by any officer thereof or of the state, including the application of moneys in the state freeway fund to the payment of the principal, interest and redemption premiums on bonds issued under this act."

The only changes made in this section since its enactment are the 1975 editorial changes (L. 1975, ch. 427, §231) to accommodate the creation of the state department of transportation.

Finally, the following provisions of K.S.A. 1982 Supp. 79-3425 concerning the state freeway fund receipts have relevance to your inquiry:

"On July 2, 1974, and on each day thereafter, after the state treasurer has received certification from the secretary of transportation that provisions have been made for the payment of the pro rata share of the amount required to be paid on the next ensuing payment date of either the principal or the interest on the outstanding highway bonds issued pursuant to K.S.A. 68-2304, the state treasurer shall

transfer from the state freeway fund to the state highway fund an amount equal to sixty-nine and twenty-three hundredths percent (69.23%) of the moneys credited to the state freeway fund on the preceding day."

In accordance with the provisions of K.S.A. 68-2301 et seq., as these sections were constituted in 1972, the state highway commission adopted a bond resolution on May 23, 1972, authorizing the issuance of the first series of highway bonds under that act. We believe the section of this resolution having particular relevance to your inquiry is Section 401, which states in pertinent part:

"A special fund is hereby created and designated 'State of Kansas Highway Bonds Interest and Sinking Fund' (herein sometimes called the 'Sinking Fund'). There are hereby created two separate accounts in the Sinking Fund designated 'Bond Service Account' and 'Redemption Account', respectively.

"The Commission covenants to withdraw from the first moneys available in the State Freeway Fund, in the manner provided by law, amounts sufficient to make the following deposits with the Fiscal Agent to the credit of said Accounts in the Sinking Fund:" (Emphasis added.)

It is within the context of these statutory and bond resolution provisions you have posed the following specific questions regarding the governor's proposal to transfer moneys from the state freeway fund to the state highway fund:

- "1. Would the proposed transfers violate the provisions of the 1972 Bond Resolution?
- "2. What actions could the bondholders take if, in their opinions, the transfer violated the provisions of the Resolution?
- "3. What would be the effect of a successful challenge on the part of the bondholders to the transfer?
- "4. Do the provisions of K.S.A. 68-2096 prevent the transfer from occurring?"

In framing your inquiry, you indicate that you suggested to the Department of Transportation during hearings of the House Committee on Ways and Means that the department "secure an

outside independent legal opinion on the Governor's proposal." Apparently in response to your suggestion, such an opinion has been provided the department, and we have been furnished a copy thereof. The opinion was prepared by Jonathan P. Small, former Assistant Attorney General and now a practicing attorney in Topeka.

We have thoroughly reviewed Mr. Small's opinion, and we concur in his legal conclusions. Accordingly, with the permission of Mr. Small and the Department of Transportation, and in order to avoid duplicating his efforts and unduly burdening our opinion, Mr. Small's opinion is attached hereto and made a part of this opinion as if fully set forth herein, with the following caveat: We are in no position to make an independent judgment as to the validity of the factual data provided Mr. Small and upon which his opinion is predicated. This office has no way of evaluating such data, including the projected revenues accruing to the state freeway fund, the current and projected balances in this fund and the debt service requirements of the issued and outstanding highway bonds. Such information, of course, is available to you as a legislator, particularly as a member of the House Committee on Ways and Means, and you also have the ability to have such data analyzed by the legislature's research staff.

Thus, for purposes of your inquiry, we believe it more appropriate for us to focus on the legal constraints on moneys in the state freeway fund. These principles, then, can provide the parameters for the legislature's consideration of the governor's proposal in light of the factual data pertaining to the freeway fund and the debt service requirements of the outstanding highway bonds. Therefore, in light of the statutory and bond resolution provisions previously discussed herein and the attached opinion of Mr. Small, we believe the following legal requirements are evident:

1. The issued and outstanding highway bonds, providing funds for the construction, reconstruction and improvement of highway projects within the state system of modern express highways and freeways, are payable solely from revenues accruing to the state freeway fund.
2. Pursuant to the statutes authorizing said bonds and the resolution providing for the issuance thereof, the secretary of transportation is authorized and required to pay the principal of and the interest on said bonds from moneys in the freeway fund, and is statutorily authorized to create reserves for such purpose.
3. Consistent therewith, the secretary of transportation is contractually obligated by the bond resolution to segregate from the first moneys available in the state freeway fund an

amount thereof, to be placed in a sinking fund, that is sufficient to make the principal and interest payments on the bonds in accordance with the bond resolution, and these payments constitute a first lien and claim on moneys accruing to the state freeway fund.

4. Pursuant to the statutes authorizing the issuance of the bonds and the bond resolution, the state has a contractual obligation to the bondholders to make the required principal and interest payments, and the legislature may not enact a law impairing this contractual obligation.

5. Thus, a law which diminishes the revenues accruing to the state freeway fund or transfers money from said fund is invalid, if it interferes with the secretary of transportation's obligation to segregate moneys in the freeway fund for the purpose of making principal and interest payments or otherwise impairs his obligation to make such payments.

6. The secretary of transportation has no authority to take action required by any such invalid law or to otherwise transfer moneys from the freeway fund until he has satisfied his obligation to ensure that principal and interest payments on the bonds may be made from the freeway fund.

We believe the foregoing principles provide the basis for resolving your first question. When these principles are applied to the factual data regarding the governor's proposed transfers of moneys in the state freeway fund to the state highway fund, including the projected revenues accruing to the freeway fund, the current and projected balances in this fund and the debt service requirements of the issued and outstanding highway bonds, the parameters of permissible legislative action respecting moneys in the freeway fund may be identified.

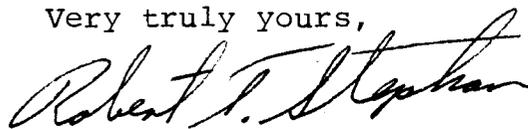
As to your questions regarding the bondholders' remedies and the potential effect of the bondholders challenging a transfer of moneys from the freeway fund, suffice it to state that the bondholders are constitutionally protected from legislation which could impair the state's contractual obligations to the bondholders. This is adequately explained in the attached opinion. Further, the statutes authorizing the issuance of the bonds and the bond resolution adopted in accordance therewith afford the bondholders specific legal remedies to protect against an impairment of the bonds' security. K.S.A. 68-2308, quoted above, authorizes various types of remedies to be included in the resolution providing for the issuance of the highway bonds, and in Article VI of the 1972 Bond Resolution submitted with your request, there are enumerated specific remedies available to the bondholders. We think it would serve little purpose here to reiterate those remedies or to speculate as to which remedy might be utilized

by the bondholders under assumed circumstances. Moreover, it is impossible for us to speculate as to the various possible effects of a "successful challenge" to a transfer of the highway fund. However, since it is implicit in your question that the bondholders' challenge to the transfer would be successful, we must presume that the ultimate effect would be a prevention of an impairment of the bonds' security.

Your final question is whether K.S.A. 68-2096 prevents the governor's proposed transfer from occurring. This statute is part of a 1973 act (L. 1973, ch. 269, §4) which authorized the construction of a toll road from Winfield, Kansas to a point on the Kansas-Oklahoma border near Baxter Springs, Kansas, the so-called Southeast Kansas Turnpike. Pursuant to K.S.A. 68-2094, the construction of this project was subject to several conditions, one of which required the project and its proposed locations to be thoroughly studied and, in effect, determined to be feasible with respect to traffic, engineering, cost and financing. It is our understanding that such study was made and that it concluded that the project was not feasible. Thus, even though K.S.A. 68-2096 has not been repealed, it is of no force or effect at this time.

In summary, therefore, it is our opinion the legislature may not enact a law which impairs the state's obligation to make the required principal and interest payments on the issued and outstanding highway bonds providing funds for the construction, reconstruction and improvement of highway projects within the state system of modern express highways and freeways. Said bonds are payable solely from the state freeway fund, and the required principal and interest payments constitute a first lien and claim on moneys accruing to said fund. Thus, even though the legislature may lawfully transfer moneys from the freeway fund to the highway fund, any law providing for such a transfer that impairs the state's contractual obligation to make the required principal and interest payments is invalid.

Very truly yours,



ROBERT T. STEPHAN
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W. Robert Alderson
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