But see 1986 Supp 75-4201

STATE OF KANSAS

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ATTORNEY GENERAL OPINION NO. 86- 13

The Honorable Joan Finney
State Treasurer
700 Harrison
P.O. Box 737
Topeka, Kansas 66601

Re: State Departments; Public Officers and Employees -- State Moneys -- Security for Deposit of State Moneys

Synopsis: K.S.A. 1985 Supp. 75-4218 provides that all state bank accounts shall be secured by a pledge of securities owned by each bank receiving a deposit. The term "securities" is defined by K.S.A. 75-4201(p)(1) to include direct obligations of, or obligations that are insured by, the United States government or one of its agencies. By virtue of 12 U.S.C. §2001 et seq., federal land banks, land bank associations, production credit associations, intermediate credit banks and banks for cooperatives are "federally chartered instrumentalities". This term has been interpreted by courts in Kansas and elsewhere as not raising them to the level of federal agencies. Accordingly, under K.S.A. 75-4201 as it now reads, obligations of these federally chartered instrumentalities may not be pledged to secure the deposit of state funds in Kansas banks. However, due to a 1983 amendment to K.S.A. 1984 Supp. 19-1402, such obligations may be used as security for the deposit of municipal funds. Cited herein: K.S.A. 1985 Supp. 9-1402; K.S.A. 75-4201; K.S.A. 1985 Supp 75-4218; L. 1983, ch. 47, §3; 12 U.S.C. §§2011, 2012, 2031, 2033, 2071, 2072, 2091, 2093, 2121, 2122, 2155, 2157.

* * *

Dear Mrs. Finney:

As Treasurer of the State of Kansas, you request our opinion concerning the application of K.S.A. 75-4201(p)(1). This statute is contained in the act which determines how state moneys shall be invested, and contains a definition of, among other terms, what constitutes a "security" under the act. This concept is significant in that any deposit of state money in a Kansas bank must be secured 100% through the pledging of acceptable securities. In view of questions which have been raised concerning certain types of securities, you request our opinion as to the legality of their use for pledging purposes.

In conversations with us, you have expressed particular concern about the use of securities issued by branches of the federal Farm Credit System. These branches include federal land banks, land bank associations, intermediate credit banks, production credit associations and banks for cooperatives, all of which are established by federal law at 12 U.S.C. §2001 et seq. While reference to such federal statutes is important in determining the legal nature of these entities, our initial examination must be of Kansas statutes, in that the latter provisions determine which securities may and may not be used for pledging purposes.

K.S.A. 1985 Supp. 75-4218 provides that all state bank accounts shall be secured by the pledging of securities equal to 100% of the amount of the account, with the securities themselves placed in the custody of the state treasurer, an approved bank or the federal reserve bank of Kansas City, Missouri. The term "securities" is extensively defined at K.S.A. 75-4201(p), and includes [at paragraph (1)]:

> "Direct obligations of, or obligations that are insured as to principal and interest by, the United States government or any agency thereof."

This definition was initially identical with one which appears at K.S.A. 1985 Supp. 9-1402(d)(1) and applies to the pledging of securities for accounts of municipal funds. However, such is no longer the case, due to changes which were made in the latter statute in 1983. At L. 1983, ch. 47, §3, K.S.A. 9-1402(d)(1) was amended by the addition of the underscored language:

> "Direct obligations of, or obligations that are insured as to principal and interest by, the United States government

or any agency thereof and obligations and securities of United States sponsored corporations which under federal law may be accepted as security for public funds."

The addition of this additional language to K.S.A. 1985 Supp. 9-1402, and its absence from K.S.A. 75-4201, becomes significant when the federal statutes are examined which create the various components of the Farm Credit System. For example, federal land banks are declared to be corporate bodies (12 U.S.C. §2012) and federally chartered instrumentalities (12 U.S.C. §2011), with a number of enumerated powers, among which is the ability to issue notes, bonds, debentures and other obligations. 12 U.S.C. §2012(10). The same types of provisions exist for the other component units of the system. Each is a federally chartered instrumentality (land bank associations -- 12 U.S.C. §2031; intermediate credit banks -- 12 U.S.C. §2071; production credit associations -- 12 U.S.C. §2091; banks for cooperatives -- 12 U.S.C. §2121), and each is empowered to issue obligations. Banks for cooperatives and intermediate credit banks may do so (like land banks) on their own initiative [12 U.S.C. §§2072(10), 2122(10)], while land bank associations and production credit associations must have prior approval from their parent land bank or intermediate credit bank [12 U.S.C. §§2033(16), 2093(12)].

Each bank is liable for obligations which it issues, as well as obligations which other banks of a similar type issue and obligations which are entered into jointly by several different types of banks or by the entire system. 12 U.S.C. §2155(a). Further, if necessary each bank may be called upon to contribute toward obligations which any other member of the system is unable to pay. It is clear, however, that the United States itself is not liable for any obligations issued by members of the system. 12 U.S.C. §2155(c).

Given the above, the provisions of K.S.A. 75-4201(p) may be examined to determine whether the component banks of the Farm Credit System fall within the definition of "security." Clearly, the obligations of banks in the system are not obligations of the United States, either directly or through insurance on principal and interest. The contribution system established by 12 U.S.C. §2155 arguably has the effect of backing the obligations of any one member of the Farm Credit System with the assets of all other members, and so may be considered as being equivalent to insurance. Thus, the single remaining question concerns whether each of the various banks is an "agency" of the United States government.

Prior to July of 1985, there were no Kansas court decisions on this question. While courts in other states had ruled, the decisions were split, with some judges ruling that an agency status did exist, with others finding that only private corporations were involved, albeit ones heavily regulated by the federal government. Typical of the former line of cases is Schlake v. Beatrice Production Credit Association, 596 F.2d 278, 281 (8th Cir. 1979), in which a federal appeals court found that a colorable claim under the Fifth Amendment due process clause was raised in a suit against a production credit association. The court noted that a production credit association is an instrumentality of the United States, and further noted that the district court had made extensive findings regarding the pervasive involvement of the federal government in the creation and operation of such associations. See also, Matter of Sparkman, 703 F.2d 1097, 1099 (9th Cir. 1983), in which the court found that a production credit association was more than a private institution with a federal charter, and so was immune from punitive damages as an instrumentality of the United States.

To the contrary is the decision in DeLaigle v. Federal Land Bank of Columbia, 568 F.2d 1432 (S.D. Ga. 1983). There, a federal district court looked to three different reasons in finding that a land bank was not an agency of the federal government. First, the court concurred with a prior decision from another Georgia federal court which found that a federally chartered corporation is not an agency unless the government has a substantial proprietary interest in it, or at least exercises considerable control over it. 568 F.2d at 1439, citing Federal Land Bank of Columbia v. Cotton, 410 F.Supp. 169 (N.D. Ga. 1975). Second, the court found that the Congressional policy behind the Farm Credit Act, as stated in 12 U.S.C. §2001, establishes that the Farm Credit System is to be farmer-owned, rather than owned by the federal government. Finally, the court determined that the federal government must be involved with the activity that causes injury in order for due process to apply, and that it was insufficient to show that the land bank was heavily regulated by the federal government. The DeLaigle decision was quoted with approval in Birbeck v. Southern New England Production Credit Association, 606 F.Supp. 1030 (D. Conn. 1985), with the court there reaching the same result, i.e. no agency, hence no due process violation.

In the case of Federal Land Bank of Wichita v. Read, 237 Kan. 751 (1985), the Kansas Supreme Court was faced with the same question, and in an unanimous decision determined to follow the DeLaigle line of decisions. As a result, it is

now the law in Kansas that federal land banks are considered to be private corporations and not governmental agencies. Given the close similarity which exists in the federal statutes between federal land banks and the other components of the Farm Credit System, it would be our opinion that the Court's holding also extends to federal land bank associations, production credit associations, banks for cooperatives and intermediate credit banks.

Accordingly, these five different types of banks do not meet the requirements for K.S.A. 75-4201(p), and their obligations may not be used by Kansas banks for security in obtaining deposits of state moneys. Given the different language which exists in K.S.A. 1985 Supp. 9-1402(d)(1), however, such obligations may continue to be used as security for the deposit of municipal funds, for it is our opinion that these banks are "United States sponsored corporations," as the term is used therein, which under federal law may have their obligations accepted as security. 12 U.S.C. §2157. Accordingly, should the legislature wish to amend K.S.A. 75-4201(p)(1), it need look no further than to the change which has already been made in the parallel statute for municipal funds.

Our conclusion herein is consistent with several prior opinions rendered by previous Attorneys General who have considered the question of what constitutes both a "security" under K.S.A. 75-4201(p) and, more specifically, an "agency" of the Federal government under paragraph (1) of that subsection. Opinion No. 78-379 dealt with a mortgage for real property which was insured by the Federal Housing Administration (FHA). Like an earlier opinion dealing with the FHA (No. 75-165), the opinion reviewed the federal statutes and regulations and concluded that an actual agency of the United States government existed. The same result was reached in Opinion No. 76-85 as to the Veterans Administration, which insured loan guaranty certificates which could be used as security for accounts containing state funds. The difference for the results reached in each of these opinions and here is directly related to the federal enabling legislation for the particular entity, i.e. is the entity created an agency of a department (such as Agriculture or Housing and Urban Development), an independent agency (like the Veterans Administration) or conversely, a federally-chartered instrumentality which is not so directly controlled.

Moreover, the one prior expression of this office which is inconsistent with the result reached herein was issued many

years prior to the Read decision, supra, which determined the status of land banks (and by analogy, other components of the Farm Credit System) in Kansas. In a one paragraph letter written by then-Attorney General Frizzell on August 22, 1969 to State Treasurer Peery, it was summarily concluded that banks for cooperatives were federal agencies. In light of Read and the decisions on which it is based, as well as the plain language of the federal statutes (12 U.S.C. §2121), we believe this letter opinion to be incorrect, and it is accordingly withdrawn.

In conclusion, K.S.A. 1985 Supp. 75-4218 provides that all state bank accounts shall be secured by a pledge of securities owned by each bank receiving a deposit. The term "securities" is defined by K.S.A. 75-4201(p)(1) to include direct obligations of, or obligations that are insured by, the United States government or one of its agencies. By virtue of 12 U.S.C. §2001 et seq., federal land banks, land bank associations, production credit associations, intermediate credit banks and banks for cooperatives are "federally chartered instrumentalities". This term has been interpreted by courts in Kansas and elsewhere as not raising them to the level of federal agencies. Accordingly, under K.S.A. 75-4201 as it now reads, obligations of these federally chartered instrumentalities may not be pledged to secure the deposit of state funds in Kansas banks. However, due to a 1983 amendment to K.S.A. 1984 Supp. 19-1402, such obligations may be used as security for the deposit of municipal funds.

Very truly yours,

Robert T. Stephan

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Jeffrey S. Southard

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RTS:JSS:crw