



STATE OF KANSAS

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ATTORNEY GENERAL OPINION NO. 86- 16

The Honorable Gayle Mollenkamp
State Representative, 118th District
Capitol Building, Room 182-W
Topeka, Kansas 66612

Re: Taxation -- Listing Property for Taxation -- Oil
and Gas Property as Personalty; Property Held by
Federal Land Bank Exempt From Taxation

Synopsis: A federal land bank is exempt from federal, state
and municipal taxation, except for taxes on real
property held by such a bank. Accordingly, a land
bank is not liable for either income or severance
tax on oil and gas which is produced on land which
it owns, or on royalty interests, leaseholds, or
wells which it owns. However, mineral interests
which have not been severed are considered as real
property, and so may be taxed. Cited herein:
K.S.A. 79-329; 79-420; 79-501; 79-1411a; 79-1439;
79-32,110; 79-4217; 12 U.S.C. §§ 2011, 2055; U.S.
Const., Art. VI, para. 2, cl. 3.

* * *

Dear Representative Mollenkamp:

As state representative to the Kansas Legislature for the
118th district, you have requested our opinion concerning
the tax status of a federal land bank. Specifically, you
inquire as to whether oil and gas production on land a federal
land bank owns is exempt from "severance, income or personal
taxes."

Federal land banks were established by Congress in 1916 and
continued by further legislation in 1971 to furnish sound,

adequate and constructive credit to agricultural producers. Each land bank is a federal instrumentality. 12 U.S.C. §2011. As such an instrumentality, it enjoys certain of the protections and privileges of the federal government, including protection from the plenary power of the state to tax and the privilege of immunity from state taxation at the discretion of Congress. Federal Land Bank v. Board of County Comrs., 368 U.S. 146, 149, 82 S.Ct. 282 7 L.Ed.2d 199 (1961); McCulloch v. Maryland, 4 Wheat 316, 4 L.Ed. 579 (1819) Congress granted this privilege to land banks in 12 U.S.C. §2055 by stating:

"Every federal land bank and every federal land bank association and the capital, reserves and surplus thereof, and the income derived therefrom shall be exempt from federal, state, municipal, and local taxation, except taxes on real estate held by a federal land bank or a federal land bank association to the same extent, according to its value, as other similar property held by other persons is taxed."

By the Supremacy Clause of the Constitution of the United States, this statute overrules any conflicting law of any state. Article VI, paragraph 2, clause 3. Accordingly, a federal land bank is subject only to Kansas taxes on real property, not personal property.

From this analysis, the crucial question becomes what is the status of oil and gas property under Kansas law. K.S.A. 79-329 states:

"For the purpose of valuation and taxation, all oil and gas leases and all oil and gas wells, producing or capable of producing oil or gas in paying quantities, together with all casing, tubing or other material therein, and all other equipment and material used in operating the oil or gas wells are hereby declared to be personal property and shall be assessed and taxed as such."

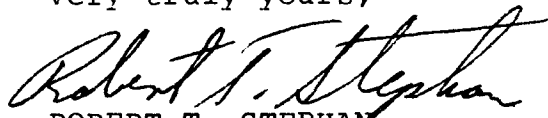
The effect of this statute is to exclude oil and gas leases and wells owned by a land bank from state taxation since, as statutorily-declared personal property, the federal statute implicitly excludes such property from state taxation. 12 U.S.C. §2055. However, in our opinion this exclusion does not extend to oil and gas mineral interests.

Oil and gas is a hybrid property interest. While in the ground and uncaptured, oil and gas mineral interests are real property and not taxable as personalty. Shaffer v. Kansas Farmers' Union Royalty Co., 146 Kan. 84, 87 (1937). However, once extracted from the natural reservoir and stored or processed, its character instantaneously changes and is considered personal property. The State of Kansas taxes, among other items, real property, income, and the severance of oil and gas. See K.S.A. 79-1439; 79-32,110; 79-4217. The first of these taxes relies on counties to assess real property for taxation (K.S.A. 79-1411a), with guidelines provided by statute in such valuation. K.S.A. 79-501. To the extent that mineral interests exist, either owned with the surface interest or separately therefrom (K.S.A. 79-420), such may be taxed as real property, even if owned by a land bank.

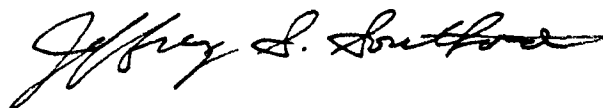
By way of contrast, income and severance taxes are imposed upon personal property. Thus, no income or severance taxes may be imposed on oil and gas royalty interests, leaseholds or actual production which is attributable to a land bank without running afoul of 12 U.S.C. §2055. See also Federal Land Bank v. Board of County Comm'rs, supra.

In conclusion, a federal land bank is exempt from federal, state and municipal taxation, except for taxes on real property held by such a bank. Accordingly, a land bank is not liable for either income or severance tax on oil and gas which is produced on land which it owns, or on royalty interests, leaseholds, or wells which it owns. However, mineral interests which have not been severed are considered as real property, and so may be taxed.

Very truly yours,



ROBERT T. STEPHAN
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Jeffrey S. Southard
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