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May 2, 1988

ATTORNEY GENERAL OPINION NO. 88- 60

William R. Halvorsen
Marshall County Attorney
Marshall County Courthouse
Marysville, Kansas 66508

Re: Taxation--Mortgage Registration and Intangibles; Mortgage Registration--Entities Subject Thereto; Bank for Cooperatives

Synopsis: Banks for cooperatives are not so closely connected to the federal government to entitle them to constitutional immunity from state taxation, nor are they exempt from payment of mortgage registration tax by virtue of 12 U.S.C.A. §2134 (West Supp. 1988). Language in Attorney General Opinion No. 87-190 indicating a contrary conclusion for production credit associations is hereby withdrawn. Cited herein: K.S.A. 79-3101; K.S.A. 1987 Supp. 79-3102; 12 U.S.C.A. §§2002, 2013, 2023, 2031, 2055, 2077, 2091, 2121, 2130, 2134 (West Supp. 1988); Pub. L. No. 99-205, 99 Stat. 1678 (1985); Pub. L. No. 100-233, 101 Stat. 1568 (1988).

* * *

Dear Mr. Halvorsen:

As Marshall County Attorney you request our opinion regarding whether the Wichita Bank for Cooperatives must pay mortgage registration fees. You inform us that the bank has taken the position that it should be exempt by virtue of its status as an instrumentality of the federal government and pursuant to 12 U.S.C.A. §2134 which specifically exempts banks for

cooperatives from the imposition of certain state and local taxes.

K.S.A. 1987 Supp. 79-3102(a) provides as follows:

> "Before any mortgage of real property, or renewal or extension of such a mortgage, is received and filed for record, there shall be paid to the register of deeds of the county in which such property or any part thereof is situated a registration fee of $.25 for each $100 and major fraction thereof of the principal debt or obligation which is secured by such mortgage, and upon which no prior registration fee has been paid."

The Kansas Supreme Court has held that the mortgage registration fee is in fact a tax rather than a fee charged for the administration work necessary in recording the mortgage. Home Owners' Loan Corp. v. Anderson, 145 Kan. 209, 210 (1937). Since the mortgage registration fee is a tax, the issue becomes whether the state may impose such a tax on banks for cooperatives.

Legal counsel for the Wichita Bank for Cooperatives informs us that the bank is a bank for cooperatives established under the Farm Credit Act of 1933, as amended. Prior to the 1988 amendments to the Farm Credit Act (Pub. L. No. 100-233, 101 Stat. 1568), the structure of the Farm Credit System could be described as follows:

> "The Farm Credit System is a network of borrower-owned cooperatives organized to provide loans to farmers and their marketing and supply cooperatives. It was established by Congress beginning in 1916 to meet the unique credit needs and problems of agricultural producers. All Government and seed money advanced was paid back to the U.S. Treasury as of 1968. The System consists of twelve Farm Credit Districts that cover the continental United States as well as Alaska, Hawaii, and Puerto Rico. Each district has a Federal land Bank, a Federal intermediate credit bank, and a bank of cooperatives:

"The Federal land Banks make long-term loans, primarily for real estate purposes, through Federal land bank associations. The Federal Intermediate credit banks provide short-and intermediate-term credit to production credit associations and other qualified financial institutions serving the production and operating needs of farmers and ranchers.

"The banks for cooperatives make loans to agricultural, aquatic, and rural utility cooperatives and provide financial services to cooperatives engaged in international trade. A thirteenth bank for cooperatives, the Central bank for Cooperatives, located in Denver, Colorado, participates with the district banks in loans that exceed district lending limits. The System is regulated by the Farm Credit Administration (FCA), an independent regulatory agency of the U.S. Government.

. . . .

"Money to finance loans made by Farm Credit banks and associations comes primarily from the sales of Farm Credit securities in the Nation's money and capital markets. . . .

"Until 1977, the three banking groups of the Farm Credit System sold their securities separately. But in 1977, consolidated system-wide bonds and notes were introduced to combine the financial strength of the System. These securities are the joint and several obligations of all 37 Farm Credit Banks, making each bank individually liable." H. Rep. No. 99-425, 1985 U.S. Code Cong. & Ad. News 2587, 2591, 2592.

"System entities are not Government owned or controlled, however the System is a 'Government sponsored entity' that affords it a preferred place in the Nation's money

> markets. System debt issuances however are not guaranteed by the Federal Government.
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> "System institutions are governed by boards of directors elected from and by System stockholders. In order to borrow from the System, a farmer must acquire stock equal to a set percentage of the loan." H. Rep. No. 100-295(I), 1987 U.S. Code Cong. & Admin. News 2723, 2726.

The Farm Credit Amendments Act, Pub. L. No. 99-205, 99 Stat. 1678 (1985), provided for the reorganization and strengthening of the Farm Credit Administration making it an "arm's-length regulator" of Farm Credit System activities. The Agricultural Credit Act, Pub. L. No. 100-233, 101 Stat. 1568 (1988), mandates an overhaul of the System organization so that it will be more efficient and competitive. See H. Rep. No. 100-295(I), 1987 U.S. Code Cong. & Adm. News 2723, 2725. Reorganization of Farm Credit System institutions pursuant to Pub. L. No. 100-233, §401 is to become effective six months after the date of enactment of these amendments, or July 6, 1988. For purposes of the issue addressed in this opinion, however, we do not believe these prospective amendments are relevant.

Two arguments are raised by the bank in support of its contention that it is exempt from payment of mortgage registration fees. We will address these arguments separately.

First, the bank contends that it is a federal instrumentality and as such is entitled to constitutional immunity from state taxation. 12 U.S.C.A. §2121 (West Supp. 1988) provides that each bank for cooperatives and its obligations are instrumentalities of the United States. In the past, the United States Supreme Court has indicated that federal instrumentalities in general, and federal land banks in particular, are immune from taxation by virtue of the perception that they perform governmental functions. See, e.g., Federal Land Bank of New Orleans v. Crosland, 261 U.S. 374, 43 S.Ct. 385, 67 L.Ed. 703 (1923); Federal Land Bank of Saint Paul v. Bismarck Lumber Co., 314 U.S. 95, 62 S.Ct. 1, 86 L.Ed. 65 (1941); Federal Land Bank of Wichita v. Board of County Commissioners, 368 U.S. 146, 82 S.Ct. 282, 7 L.Ed.2d 199 (1961). However, in 1982 the Supreme Court clarified the doctrine of federal immunity from state taxation:

"With the famous declaration that 'the power to tax involves the power to destroy,' McCulloch v Maryland, 4 Wheat 316, 431, 4 L Ed 579 (1819), Chief Justice Marshall announced for the Court the doctrine of federal immunity from state taxation. In so doing he introduced the Court to what has become a 'much litigated and often confused field,' United States v City of Detroit, 355 US 466, 473, 2 L Ed 2d 424, 78 S Ct 474 (1958), one that has been marked from the beginning by inconsistent decisions and excessively delicate distinctions.

. . . .

"We have concluded that the confusing nature of our precedents counsels a return to the underlying constitutional principle. The one constant here, of course, is simple enough to express: a State may not, consistent with the Supremacy Clause, U.S. Const, Art VI, cl 2, lay a tax 'directly upon the United States.' Mayo v United States, 319 US 441, 447, 87 L Ed 1504, 63 S Ct 1137, 147 ALR 761 (1943). While '[o]ne could, and perhaps should, read M'Culloch . . . simply for the principle that the Constitution prohibits a State from taxing discriminatorily a federally established instrumentality,' First Agricultural Bank v State Tax Comm'n, 392 US 339, 350, 20 L Ed 2d 1138, 88 S Ct 2173 (1968) (dissenting opinion), the Court has never questioned the propriety of absolute federal immunity from state taxation.

. . . .

"But the limits on the immunity doctrine are, for present purposes, as significant as the rule itself. Thus, immunity may not be conferred simply because the tax has an effect on the United States, or even because the Federal Government

shoulders the entire economic burden of the levy.

. . . .

"Similarly, immunity cannot be conferred simply because the state tax falls on the earnings of a contractor providing services to the Government. . . . Indeed, immunity cannot be conferred simply because the tax is paid with Government funds;

. . . .

"What the Court's cases leave room for, then, is the conclusion that tax immunity is appropriate in only one circumstance: when the levy falls on the United States itself, or on any agency or instrumentality so closely connected to the Government that the two cannot realistically be viewed as separate entities, at least insofar as the activity being taxed is concerned. This view, we believe, comports with the principal purpose of the immunity doctrine, that of forestalling 'clashing sovereignty,' McCulloch v Maryland, 4 Wheat, at 430, 4 L Ed 579, by preventing the States from laying demands directly on the Federal Government. See City of Detroit v Murray Corp. 355 US, at 504-505, 2 L Ed 2d 441, 78 S Ct 458 (opinion of Frankfurter, J.). As the federal structure--along with the workings of the tax immunity doctrine--has evolved, this command has taken on essentially symbolic importance, as the visible 'consequence of that [federal] supremacy which the constitution has declared.' McCulloch v. Maryland, 4 Wheat, at 436, 4 L Ed 579. At the same time, a narrow approach to governmental tax immunity accords with competing constitutional imperatives, by giving full range to each sovereign's taxing authority. See Graves v. New York

> ex rel. O'Keefe, 306 U.S. at 483, 83 L Ed 927, 59 S Ct 595, 120 ALR 1466.
>
> "Thus, a finding of constitutional tax immunity requires something more than the invocation of traditional agency notions: to resist the State's taxing power, a private taxpayer must actually 'stand in the Government's shoes.' City of Detroit v Murray Corp. 355 US, at 503, 2 L Ed 2d 441, 78 S Ct 458 (opinion of Frankfurter, J.)." United States v. New Mexico, 455 U.S. 720, 102 S.Ct. 1373, 71 L.Ed.2d 580, 589, 591, 593 (1982). (Emphasis added.)

Thus, we must determine whether a bank for cooperatives is an "instrumentality so closely connected to the Government that the two cannot realistically be viewed as separate entities." The Bismarck Court, supra, implied that all activities of federal corporations constitute governmental action. 314 U.S. at 102. "However, this statement from a 1941 case seems to be in conflict with . . . the general trend to restrict the parameters of what constitutes governmental action." LPR Land Holdings v. Federal Land Bank of Saint Paul, 651 F.Supp. 287, 292 (E.D. Mich. 1987). Since the Court's holding in Bismarck, various jurisdictions have concluded that federal land banks and production credit associations are more like private corporations than federal agencies for various purposes. See, e.g., Federal Land Bank of Columbia v. Cotton, 410 F.Supp. 169 (N.D. Ga. 1975) (federally chartered corporation is not an "agency" unless the government has a substantial proprietary interest in it, or at least exercises considerable control over operation and policy of the corporation; held federal land bank was meant to be private, rather than governmental, corporation for purposes of federal district court jurisdiction); DeLaigle v. Federal Land Bank of Columbia, 568 F.Supp. 1432 (S.D. Ga. 1983) (federal land bank was private corporation without sufficient governmental involvement to support cause fo action under federal due process clause); Birbeck v. Southern New England Production Credit Association, 606 F.Supp. 1030 (D.Conn. 1985) (production credit association considered private entity rather than governmental agency for purposes of invoking federal due process clause); Federal Land Bank of St. Louis v. Keiser, 628 F.Supp. 769 (D.C. Ill. 1986) (federally chartered land bank not "agency" of federal government for purposes of removal jurisdiction); Redd v. Federal Land Bank of St. Louis, 661 F.Supp. 861 (E.D. Mo.

1987) (acts of federal land bank not acts of federal government for purposes of 5th Amend. due process). The Supreme Court of Kansas has expressly adopted this line of decisions for purposes of determining entitlement to due process. Federal Land Bank of Wichita v. Read, 237 Kan. 751, 755 (1985).

While the above-cited cases pertain to the identity of federal land banks and production credit associations for purposes other than taxation, we find them relevant in that they stand for the proposition that these Farm Credit System institutions are entities separate and distinct from the federal government in many respects, and that heavy federal regulation alone is not sufficient to transform a private entity into an arm of the federal government for all purposes. The Farm Credit Act and amendments further evidence the separation between Farm Credit System institutions and the federal government. These institutions are owned and controlled by System borrowers, not the government. 12 U.S.C.A. §§2013, 2031, 2091, 2130 (West Supp. 1988). The Farm Credit Administration, a federal agency, now functions as an arm's-length regulator of the System rather than supervising day to day System management. 12 U.S.C.A. §2002 (West Supp. 1988).

Based on the current structure of the Farm Credit System and the foregoing case law, it is our opinion that Farm Credit System institutions, including banks for cooperatives, are not so closely connected to the federal government as to afford them constitutional immunity from state taxation. In so concluding, we acknowledge the Kansas Supreme Court's holding in Home Owners' Loan Corporation v. Anderson, 145 Kan. 209 (1937), and find it distinguishable. In Anderson the court held that "as operated at the present time the Home Owners' Loan Corporation is an instrumentality of the federal government comparable to the United States Bank dealt with in McCulloch v. State of Maryland, 4 Wheat 316. The United States supreme court has held that such instrumentalities were not required to pay tax on mortgages offered for registration." (Emphasis added.) We submit that, as currently operated, banks for cooperatives, federal land banks and production credit associations are not federal instrumentalities comparable to the United States bank dealt with in McCulloch v. Maryland.

This is not to say that Congress could not, if it so chose, grant immunity to these institutions through properly enacted legislation. United States v. New Mexico, 455 U.S. at 737, 71 L.Ed.2d at 594. Congress has in fact done so for federal

land banks. 12 U.S.C.A. §2055, codified at 12 U.S.C.A. §2023 (West Supp. 1988) beginning six months after January 6, 1988.

Legal counsel for the Wichita Bank for Cooperatives contends that the bank has similarly been granted exempt status by 12 U.S.C.A. §2134 which provides:

> "Each bank for cooperatives and its obligations are instrumentalities of the United States and as such any and all notes, debentures, and other obligations issued by such bank shall be exempt both as to principal and interest from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States or any State, territorial, or local taxing authority, except that interest on such obligations shall be subject to Federal income taxation in the hands of the holder." (West Supp. 1988).

While this provision exempts the bank's obligations from taxation (except surtaxes, estate, inheritance and gift taxes), it does not exempt the bank's assets. A mortgage which secures a note evidencing a loan made by the bank is not an obligation of the bank, but an asset. It is therefore our opinion that 12 U.S.C.A. §2134 does not operate to exempt the Wichita Bank for Cooperatives from payment of the mortgage registration tax.

You point out that this office reached a contrary conclusion in regard to production credit associations. Attorney General Opinion No. 87-190. Given the close similarity which exists in the federal statutes between production credit associations and banks for cooperatives [the taxation provisions are nearly identical, 12 U.S.C.A. §§2077 and 2134 (West Supp. 1988)], we withdraw the language in Attorney General Opinion No. 87-190 which indicates a contrary conclusion for production credit associations.

In conclusion, banks for cooperatives are not so closely connected to the federal government to entitle them to constitutional immunity from state taxation, nor are they exempt from payment of mortgage registration tax by virtue of 12 U.S.C.A. §2134 (West Supp. 1988). Language in Attorney

General Opinion No. 87-190 indicating a contrary conclusion for production credit associations is hereby withdrawn.

Very truly yours,

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