STATE OF KANSAS

OFFICE OF THE ATTORNEY GENERAL

2ND FLOOR, KANSAS JUDICIAL CENTER, TOPEKA 66612-1597

ROBERT T. STEPHAN
ATTORNEY GENERAL

June 20, 1991

MAIN PHONE: (913) 296-2215
CONSUMER PROTECTION: 296-3751
TELECOPIER: 296-6296

ATTORNEY GENERAL OPINION NO. 91- 66

H. Douglas Pfalzgraf
General Counsel
Attica District Hospital
522 N. Washington
P.O. Box 668
Wellington, Kansas 67152-0668

Re: Townships and Township Officers -- Hospital and Health Care Facilities; Hospitals -- Lease of Hospital Property; Oil/Gas Lease; Operating Expenses of Oil/Gas Well

Synopsis: Under the facts presented, the board of a hospital district organized under K.S.A. 80-2501 et seq., which has become a working interest owner pursuant to the terms of an oil and gas lease, has the authority to expend hospital monies, not otherwise committed, for payment of oil and gas well expenses. Cited herein: K.S.A. 1990 Supp. 12-1675; K.S.A. 80-2501; 80-2517.

* * *

Dear Mr. Pfalzgraf:

As general counsel for Attica District Hospital No. 1, you ask our opinion regarding whether a district hospital as a working interest owner may expend public money for payment of oil and gas well expenses.

You inform us that Attica District Hospital No. 1 was organized as a hospital district pursuant to K.S.A. 80-2501

et seq. In 1981 the hospital entered into an oil and gas lease with a private oil and gas company in relation to real property the hospital owns in Harper county. The lease provided that the hospital would initially receive 3/16th royalty interest payments. Pursuant to the lease the hospital would not be responsible for operating expenses for oil and gas production until such time as the company investors recouped four times their original investment. This event came about in 1984 at which time, according to the terms of the lease, the entire working interest of the wells less a 1/16 override reverted to the hospital which then assumed responsibility for expenses incurred in the normal operation of the wells (e.g., pumpers, electricity, ad valorem taxes).

For some years the wells were immensely profitable to the hospital with income exceeding operating expenses. However, more recently, production of the wells has leveled off and certain re-working expenses have been incurred as a matter of necessity. As a result income from the wells has barely kept pace with expenses and at times expenses have actually exceeded income from the wells.

The hospital has now received two bids from interested private parties who desire to purchase the working interest in the wells from the hospital as those parties believe that the wells may again be profitable. The hospital also believes that the wells may again be profitable and therefore would like to determine whether or not, as a matter of law, continued ownership in the working interest is permissible so that all options may be fully considered.

It is this situation which has prompted your question of whether the hospital district as a working interest owner may expend hospital moneys for payment of oil and gas well expenses.

K.S.A. 80-2517 sets forth the statutory contracting authority of the hospital board in relation to leases of hospital property to other entities, leases of real and personal property from other entities and the management of the hospital. Section (a)(1) of that statute provides:

> "The board may enter into written contracts for the lease of any hospital property to any person, corporation, society or association upon such terms and

conditions as deemed necessary by the board."

While only recently have the well operating expenses outdistanced its income, the hospital has in fact been paying operating expenses as a working interest owner since 1984. The question is thus not whether the hospital may retain its working interest in light of the recent well unprofitability, but whether the hospital was authorized to enter this lease in the first place.

Despite the broad language in K.S.A. 80-2517(a)(1) authorizing the hospital board to lease "any hospital property . . . upon such terms and conditions as deemed necessary by the board," case law provides limitations to that grant of authority. To determine its legality, a lease must be evaluated against those limitations.

First, the "terms and conditions deemed necessary by the board" must be those which are necessarily implied within the general grant of authority to enter a written contract for the lease of hospital property. The general rule is that when powers are expressly conferred the power is implied to take such reasonable means as may be necessary for the effective exercise of the powers conferred and the discharge of duties imposed. Edwards County Commissioner v. Simmons, 159 Kan. 37, 53 (1944), citing State, ex rel., v. Younkin, 108 Kan. 634 (1922). Like other corporations, hospitals have all the powers expressly conferred on them by charter, or by the general law under which they are organized, and such other powers as are incident or necessary to the execution of their express powers. 40 Am.Jur.2d Hospitals and Asylums, § 5 (1968). See also 41 C.J.S. Hospitals, § 6 (1991). The express grant of a power may result in the implied power to create indebtedness for the exercise of that power. See 15 McQuillin, Municipal Corporations, § 39.17 (3d Ed. 1985), citing City of Wichita v. Wyman, 158 Kan. 709 (1944).

In the instant situation the question thus becomes whether the provision in the oil and gas lease executed by the board in 1981 which committed the board to future payment of operating expenses was within the board's authority as a power necessarily implied by the express power to lease hospital property. Whether or not the hospital acted wisely regarding this term of the lease is not the question. The issue is whether the board had authority to do so. In our opinion the board did have such authority because in order for the hospital to exercise its power to enter this type of lease,

provision had be to be made for the payment of operating expenses of the wells. Therefore, in our opinion, the power to make provision for the payment of such expenses is an implied power necessarily flowing from the express power of the hospital board to enter into written contracts for the lease of hospital property upon such terms and conditions as deemed necessary by the board.

Evaluating the lease against this first common law criteria, we opine that the board as a working interest owner, had and still has the authority to expend hospital monies, not otherwise committed, for payment of oil and gas well expenses.

Second, the hospital board has the responsibility for the management and control of the hospital and accordingly has exclusive control of the expenditures of all hospital monies. K.S.A. 80-2511. Ulrich v. Board of County Commissioners of Thomas County, 234 Kan. 782 (1984), discusses the rule that expenditures of public monies must be for a legitimate public purpose, which will not be defeated merely because the execution of it involves payments to individuals, or private corporations. In its discussion of "public purposes," the court stated:

> "It has been said that a strict formula to determine public purposes for all times cannot be formulated, since the concept expands with the population, economy, scientific knowledge, and changing conditions. As people are brought closer together in congested areas, the public welfare requires governmental operations of facilities which were once considered exclusively private enterprise, and necessitates the expenditure of tax funds for purposes which were not classified as public. What is a public purpose for which public funds may be expended is not a matter of exact definition, and the line of demarkation is not immutable or incapable of adjustment to changing social and economic conditions that are properly of public and governmental concern." Ulrich at p. 789.

The Ulrich court then quoted Leavenworth Co. v. Miller, 7 Kan. 479 (1871) from Syl. 13:

> "The government may accomplish a public purpose through the means of a private agency, a private individual or individuals, or a private corporation. It is the ultimate object to be obtained which must determine whether a thing is a public or a private purpose."

Further guidance regarding whether a contract (in this case a lease) is within public policy limits is found in Edwards County Commissioners v. Simmons, 159 Kan. 37, 54 (1944), citing Fisk v. Board of Managers, 134 Kan. 394 (1931). There, the court stated that if a contract is reasonable, prudent and economically sound it is not contrary to public policy.

In addition, Attorney General Opinions No. 88-42, 87-164 and 80-19 also discuss the public purpose doctrine and reiterate the general rule that public monies cannot be used merely to aid a private entity or enterprise, however laudable its purpose or useful its encouragement. Whether a particular expenditure serves a public or private purpose is often a question of fact properly decided by the authority given the discretion to make that decision or a court of law.

> "The power to lease is a purely discretionary function entrusted to the elected officials of the local government and, absent a clear abuse of that discretion, any decision made by them will not be overturned." McQuillan Mun. Corp. § 28.42 (3rd Ed.).

While we cannot conclusively settle what is ultimately a question of fact, from the information provided it does not appear that in your situation the oil and gas lease which committed hospital expenditures towards oil and gas well operating costs would be outside legitimate public purpose expenditures. The ultimate object of such expenditures is, we assume, to generate additional income for the hospital. Whether the oil/gas lease entered into by the hospital was a reasonable, prudent and economically sound contract is, however, purely a question of fact.

In addition, we note that income received by the hospital as owner of the working interest of the well would be "hospital monies" as defined by K.S.A. 80-2501(c), i.e. "monies

acquired through . . ." and as such are subject to the expenditure and investment requirements of K.S.A. 80-2517(c):

> "Hospital monies shall be deemed public monies and hospital monies not immediately required for the purposes for which acquired may be invested in accordance with the provisions of K.S.A. 12-1675 and amendments thereto. . . ."

The statutory prohibition against certain types of investments found in K.S.A. 12-1675 is applicable to monies acquired by the hospital, i.e. the hospital may not use hospital monies to invest in oil and gas wells. Here, however, the hospital did not invest in the wells. The hospital owned real property, a portion of which was leased to a private company in which others invested. In the event of a producing well, the hospital would and did financially benefit. Those financial benefits which flow from the oil and gas lease are hospital monies subject to the provisions of K.S.A. 80-2517(c) and K.S.A. 12-1675.

In conclusion, assuming that the oil/gas lease was entered into for a legitimate public purpose, under the facts presented, the board of a hospital district organized under K.S.A. 80-2501 et seq., which has become a working interest owner pursuant to the terms of an oil and gas lease has the authority to expend hospital monies, not otherwise committed, for payment of oil and gas well expenses.

Very truly yours,

Robert T. Stephan

ROBERT T. STEPHAN
ATTORNEY GENERAL OF KANSAS

Camille Nohe

Camille Nohe
Assistant Attorney General

RTS:JLM:CN:bas