

MINUTES OF THE HOUSE COMMITTEE ON LOCAL GOVERNMENT.

The meeting was called to order by Chairman Vickrey at 3:30 p.m. on January 23, 2003 in Room 519-S of the Capitol.

All members were present except:

Committee staff present:

Mike Heim - Legislative Research Department  
Kathie Sparks - Legislative Research Department  
Theresa Kiernan - Office of Revisor of Statutes  
Maureen Stinson - Committee Secretary

Conferees appearing before the committee:

Rep. Tom Sloan, District 45, Kansas House of Representatives  
Elmer Ronnebaum, General Manager, Kansas Rural Water Association  
Neil Dobler, Director of Public Works, City of Topeka  
Don Rankin, Director of Water Supply, City of Topeka  
Gayle Bayless, Manager, Shawnee County Rural Water District #7  
Gary Hanson, Attorney, Shawnee County Rural Water District #7  
Derl Treff, Director of Investments, Pooled Money Investment Board, State of Kansas  
Janis C. Bunker, Sr. V.P. & Trust Officer, Trust Co. of Kansas  
Craig Jordan, President, Index Powered CD  
Eric Donaldson, Asst. V.P. & Controller, Silver Lake Bank  
John J. Haas, President, Ranson Financial Consultants, LLC, Wichita

Others attending:

See attached list

The Chairman opened the hearing on:

**HB 2003: Rural water supply districts; acquisition of system by adjoining municipality**

Rep. Tom Sloan addressed the committee in support of the bill (Attachment 1). He stated that the reason this bill is before the committee is because there has to be a way to legally transfer assets, assume customer billing responsibilities and the continuation of service when a rural water district is acquired in whole by a city. He explained that the bill was requested to facilitate the acquisition of a Shawnee County Rural Water District by the City of Topeka.

Chair introduced another proponent, Elmer Ronnebaum, General Manager, Kansas Rural Water Association (Attachment 2). He said that a rural water system may want to get out of the business of being a rural water system because smaller communities are facing increasingly complex regulations and requirements. As a representative of the Kansas Rural Water Association, he asked that the committee give favorable support of the bill.

Neil Dobler, Director of Public Works, City of Topeka, appeared next before the committee to speak in favor of the bill (Attachment 3). He informed the committee that although the rural water district and the city agree on acquisition terms, it appears that adequate legislation is not in place to allow them to proceed. He stated that the bill under consideration would remedy that situation. On behalf of the Mayor and the Department of Public Works, he asked for the committee's support of the bill.

Also testifying in favor of the bill was Don Rankin, Director of Water Supply, City of Topeka (Attachment 4). He expressed that the bill offers the opportunity for the rural water district and the city to work together for the common good of their customers without obligating either party to accept undesirable conditions. He stated that the bill does not create the opportunity for hostile takeovers of rural water districts by cities nor obligate a cities to merge a rural water district into the city's system. Mr. Rankin explained that the bill also creates clear legal means to merge a rural water district system within the city system. On behalf of the Mayor and the City of Topeka, he asked for the committee's support of the bill.

CONTINUATION SHEET

MINUTES OF THE HOUSE COMMITTEE ON LOCAL GOVERNMENT at on January 23, 2003 in Room 519-S of the Capitol.

Gayle Bayless, Manager, Shawnee County Rural Water District #7, testified in support of the bill (Attachment 5). She stated that reduced water bills and full time active management by the City of Topeka would be a huge benefit to the patrons of the district. On behalf of Shawnee County Rural Water District #7, she asked the committee for favorable action on this bill.

The last proponent, Gary Hanson, Attorney, representing Shawnee County Rural Water District #7, testified (Attachment 6). He explained that the bill is modeled after K.S.A. 19-3512, a statute concerning Water Supply and Distribution Districts, under which Water District No. 1 in Johnson County has successfully annexed territory and acquired water systems on several occasions. He stated that there are instances where considerable efficiency can be obtained by merging a small water system like Rural Water District #7 into a larger one. He urged favorable support of the bill.

There were no opponents to the bill.

Chairman Vickrey closed the hearing on **HB 2003**.

Chairman Vickrey opened the hearing on:

**HB 2011: Investments of public moneys; duration; equity-linked certificates of deposit**

Rep. Tom Sloan spoke in support of the bill and informed the committee that the bill has two components: first, equity-linked certificates of deposit are authorized as an investment option and second, the time for which municipalities may invest idle funds is extended from two to five years (Attachment 7). He stated that equity-linked certificates of deposit and the bill are not a "threat" to the Pooled Money Investment Board. He asked the committee members to give local officials another tool with which to manage their responsibilities on behalf of the citizens of Kansas.

Speaking next as a proponent of the bill was Janis C. Bunker, Sr. V.P. & Trust Officer, Trust Co. of Kansas (Attachment 8). She said that equity linked certificates of deposit would give local government organizations the ability to enjoy the growth found in equity investments with no exposure to loss for their principal. She further stated that when local government purchases an equity linked CD at their local bank, it also benefits that bank since the money remains in the community.

Craig Jordan, President, Index Powered CD, testified in favor of the bill (Attachment 9). He submitted that the ability to offer the equity linked CD product to local municipal or other public units by Kansas community banks could provide a conduit to maintain additional local funds in the community. He urged that the additional source of funds deposited in the community bank for the 5 year period of time assists bankers in meeting the needs of the community while offering the public unit additional investment opportunities.

Another proponent, Eric Donaldson, Asst. V.P. & Controller, Silver Lake Bank explained to the committee that the bill would further support the growth of critically needed longer term core deposits in Kansas community financial institutions (Attachment 10). He expressed that the bill opens new avenues for local governmental entities, Kansas financial institutions and Kansas communities.

John J. Haas, President of Ranson Financial Consultants, testified in support of the bill with certain amendments (Attachment 11). He recommends that local units of government be allowed to invest with local credit unions since the NUCA is similar to the FDIC. His major concern about the bill is allowing local units of government to invest in equity-linked certificates of deposit. He summarized that he would like to see the bill passed with amendments adding credit unions as an authorized investment provider and the removal of equity-linked CD's as an authorized investment.

Derl Treff, Director of Investments, Pooled Money Investment Board, State of Kansas, appeared before the committee as the sole opponent to the bill (Attachment 12). He expressed concern that the inclusion of equity-linked certificates of deposit as an investment option for municipalities would significantly increase the risk level of a municipality's investment portfolio. He submitted that providing this as an

CONTINUATION SHEET

MINUTES OF THE HOUSE COMMITTEE ON LOCAL GOVERNMENT at on January 23, 2003 in Room 519-S of the Capitol.

investment alternative to all cities, counties, school districts, rural water associations, fire districts, community colleges etc. in the State of Kansas would be a significant departure from the risk characteristics of the current investment options (U.S. treasuries, Kansas bank CD's and the Kansas Municipal Investment Pool). He states that the varying levels of financial expertise within each municipality compound this risk.

The Chairman closed the hearing on **HB 2011**.

Rep. Kassebaum submitted a bill request to the committee concerning township roadways. Without objection, it will be introduced as a committee bill.

Don Moler, League of Kansas Municipalities, presented two bill requests. He stated that the first request concerns legal publications on the internet. He informed the committee that the second request relates to idle fund investments in Non-Kansas Chartered Banks. Without objection, both bill requests will be introduced as committee bills.

The meeting was adjourned at 4:55 P.M.

The next meeting is scheduled for January 28.

**HOUSE LOCAL GOVERNMENT**

**DATE** 1-23-03

<b>NAME</b>	<b>REPRESENTING</b>
DON RANKIN	CITY OF TOPEKA
Neil Dobler	City of Topeka
Elmer Romebaum	Ks Rural Water Assoc.
John Haas	Ransom Financial
David Shupe	" "
Amy Johnson	RWD #7 S.W. Co.
Gayle Bayless	RWD #9 S.W. Co.
Erik Sartorius	City of Overland Park
Von Sloan	Leg.
Cros Jordan	
D	

JM SLOAN  
 REPRESENTATIVE, 45TH DISTRICT  
 DOUGLAS COUNTY

STATE CAPITOL BUILDING  
 ROOM 446-N  
 TOPEKA, KANSAS 66612-1504  
 (785) 296-7677  
 1-800-432-3924

772 HWY 40  
 LAWRENCE, KANSAS 66049-4174  
 (785) 841-1526  
 sloan@house.state.ks.us



TOPEKA

HOUSE OF  
 REPRESENTATIVES

COMMITTEE ASSIGNMENT  
 CHAIRMAN: HIGHER EDUCATION  
 MEMBER: UTILITIES  
 ENVIRONMENT  
 GENERAL GOVERNMENT &  
 HUMAN RESOURCES  
 BUDGET

## TESTIMONY ON HB 2003 – LOCAL GOVERNMENT COMMITTEE

Thank you, Mr. Chairman. Members of the Committee, I am chairman of Douglas County Rural Water District #1 and have over the past 20 years helped write most of the laws related to city-rural water district relations – especially those concerning annexations of RWD customers and facilities. Statutes exist to compensate water districts for the loss of patrons when a city expands, for the merger of two rural water districts, and for the formation of public wholesale water districts.

However, no procedure exists for a rural water district to be acquired in whole by a city. The statute that permits a rural water district to disband, does not address this situation because the city would have no way to acquire the district's capital equipment, patron billing information, etc. Similarly, when a city annexes part of a district, a water district board of directors exists to receive the compensation and continue serving the remaining customers, but no legal entity would exist if the entire district were annexed.

HB 2003 authorizes a city to acquire and operate the assets of a rural water district and provides a process by which the district's board of directors and city commissioners must publicly approve the acquisition. In addition, the bill establishes public notification and protest petition process so that district patron interests are protected. The bill further requires the city to provide information about rates, new connection policies, and other operational matters to protect rural water district patron interests. The bill does not permit the "hostile" take-over of rural water districts by cities.

HB 2003 was requested to facilitate the acquisition of a Shawnee County RWD by the City of Topeka. Both the rural water district's board of directors and the City desire the acquisition to proceed. Other conferees will provide additional specific information on that situation. My sponsorship of HB 2003 is simply to permit RWD boards of directors to best serve their constituencies in partnership with their urban colleagues to cost-effectively protect public health, while wisely managing a natural resource and patron interests.

I encourage you to recommend HB 2003 favorably for passage.

House Local Government  
 Date: 1-23-2003  
 Attachment # 1



P.O. Box 226 • Seneca, KS 66538 • 785/336-3760  
FAX 785/336-2751 • <http://www.krwa.net>

COMMENTS ON HOUSE BILL No. 2003  
BEFORE THE HOUSE COMMITTEE ON LOCAL GOVERNMENT  
January 23, 2003

Mr. Chairman and Members of the Committee:

I am Elmer Ronnebaum, General Manager for the Kansas Rural Water Association. I appreciate the opportunity to submit comments on HB 2003.

The Kansas Rural Water Association provides training and technical assistance to municipal and rural water systems and also to municipal wastewater utilities.

HB 2003 would provide a vehicle whereby rural water districts that come to such agreement might transfer their assets to a municipality. Small rural water districts might do this for two reasons: 1) to gain a great efficiency in operations by merging their water utility with the municipal system and 2) to allow for the orderly expansion of cities wishing to annex an entire rural water district.

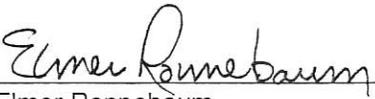
Present Kansas law provides for the consolidation of individual rural water districts and it also provides for the merger of rural water districts with Water One in Johnson County. In fact, four original rural water districts have merged with Water One, the last most recently in November 2002.

HB 2003 would allow for a rural water district to transfer its assets to a city if both the district and city come to such agreement. We believe that the proposed bill has sufficient provisions for protection to the water district's customers as the legislation contains requirements for notification of all customers of any intent to merge with the municipality. There is sufficient authority for annexation and compensation to rural water districts in those cases where a city may desire to only annex a portion of the district. HB 2003 addresses those situations where the entire rural water district would be assumed by the city.

Smaller water systems are being ever challenged in their ability to meet the increased demands for technical and financial capacity. Kansas Rural Water Association believes it is in the public interest that small rural water districts that can come to agreement with a municipality be allowed to transfer their assets to that municipality. HB 2003 would grant the tool to accomplish such mergers.

The Kansas Rural Water Association respectfully urges favorable consideration of HB 2003.

Respectfully submitted,

  
Elmer Ronnebaum  
General Manager

House Local Government  
Date: 1-23-2003  
Attachment # 2



# CITY OF TOPEKA

---

Department of Public Works • Administration  
515 S. Kansas Avenue 4th Flr.  
Topeka, Kansas 66603-3422  
Phone 785-368-3801  
Fax 785-368-3806

January 23, 2003

Jene Vickrey, Chairman  
House Committee on Local Government  
300 SW 10<sup>th</sup> St, Room 115 South  
Topeka, KS 66612

RE: Testimony in Support of House Bill 2003

Dear Chairman Vickrey and Members of the Committee:

I am the Director of Public Works for the City of Topeka. I am here with Mr. Don Rankin, the Manager of Topeka Water, a Division of the Public Works Department, to testify in favor of House Bill 2003.

Last year, after learning that Rural Water District No. 7, a district that borders the south city limits, was interested in merging with another water supplier, we began discussions with them concerning acquisition of RWD 7 by the City of Topeka.

As our discussions commenced, it became apparent that the acquisition would be a win-win situation for both entities. The City is currently engaged in a major economic development initiative in that area and has plans to enhance the water infrastructure in that zone to facilitate future intense development. The District has been well-run and provided excellent service to their customer/owners, but has focused primarily on residential service. As some of this area transitions to more industrial use, the Topeka Water is in a better position to fund the necessary infrastructure improvements.

In the course of our discussions, it also became apparent that acquisition by the City of Topeka would result in a substantial reduction in the average monthly water bill for the District's customers.

House Local Government  
Date: 1-23-2003  
Attachment # 3

Even though both the District and the City agree on the acquisition terms, it appears that adequate legislation is not in place to allow us to proceed. The bill under consideration would remedy that situation. On behalf of the Mayor and the Department of Public Works, I ask for your support of House Bill 2003.

Sincerely,



Neil Dobler, PE  
Director

cc: Mayor Felker  
Dave Graversen, CAO  
Don Rankin



# CITY OF TOPEKA

---

Water Division  
3245 Waterworks Drive  
Topeka, Kansas 66606

January 23, 2003

Chairman Vickrey  
House Committee on Local Government

RE: TESTIMONY IN SUPPORT OF HOUSE BILL 2003

Dear Chairperson Vickrey and Members of the Committee on Local Government:

I am the Manager of Topeka Water, a Division of the City Public Works Department and I am here with Mr. Neil Dobler, Director of Public Works for the City of Topeka to testify in support of HB 2003.

The City of Topeka Water Division provides water to the entire City of Topeka and surrounding area including 9 wholesale customers of which 8 are Rural Water Districts. These Rural Water Districts, in-turn, resell the water to other communities and other Rural Water Districts. We are a regional water supplier providing water to most of Shawnee County, much of Jackson and Osage Counties as well as some parts of Douglas and Wabaunsee Counties. We conservatively estimate that over 150,000 Kansans are served with water produced at the Topeka Water Treatment Plant.

The desire to merge a Rural Water District system into a City system should be no surprise. Rural Water Districts (RWDs) were created under K.S.A. 82a-612 et seq. to serve a need for water in rural communities. Some of these rural communities were established in close proximity to larger Cities such as Topeka. The RWD tends to enjoy a larger customer base being located next to a City but with urban growth, Cities tend to extend their limits into the RWD boundaries. If and when City limits expand into an area served by a RWD, the following issues need to be resolved or acknowledged:

- The RWD will have less revenue to support their operations
- The City will likely need to provide fire protection with water lines that may be undersized to provide fire service. Costly water line replacements would have to be installed as well as new fire hydrants.
- If RWD assets such as treatment plants, pump stations or water towers are in an area acquired through City growth, it may not be clear as to who owns, operates

House Local Government  
Date: 1-23-2003  
Attachment # 4

Chairperson Vickrey

January 23, 2003

Page 2

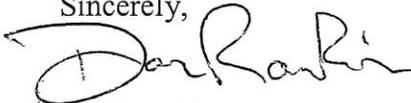
- and maintains the assets. This creates situations where expensive resources are inefficiently deployed as each tries to reliably serve their customer base.
- It may be difficult for the RWD or City to serve certain customers without using infrastructure owned by the other entity.
- Dead end water mains may become operational problems for both the RWD and the City.
- Complex metering arrangements between the City and the RWD may be required to provide water to the remaining RWD customers.

HB2003 offers the opportunity for the RWD and the City to work together for the common good of all of their customers without obligating either to accept undesirable conditions. HB2003 does not create the opportunity for a City to perpetrate an unfriendly acquisition of a RWD nor does it obligate a City to merge a Rural Water District into the City's system. HB2003 does create the clear legal means to merge a RWD into a City system when both parties agree it is for the best interest of their respective customers.

Even if urban growth and extension of City limits into a RWD is not an issue between the RWD and the City, it may still be in the best interest of the RWD and the City to merge the RWD into the City system. The City system usually has more resources to serve customers in the best and most economical manner, allowing the City to serve the area, unencumbered, for economic development.

HB2003 provides Cities and RWDs the ability to remedy problems before they occur and to harbor an atmosphere of trust and cooperation as they work together for the greater good of their customers. On behalf of the Mayor and the City of Topeka, I ask for your support of House Bill 2003.

Sincerely,



Don Rankin

Water Superintendent

Cc: Mayor Felker  
Dave Graversen, CAO  
Neil Dobler, Director of Public Works

1-23-2003

House Bill 2003

Shawnee County Rural Water District #7

This rural water district possesses a very well built water distribution system. The cost of the improvements to this system, which were performed in the early 1990's, is such that our customers pay very high water rates. Our rates are among the highest in northeast Kansas.

The City of Topeka wishes to acquire this water system. With their large customer base, they can absorb that cost, and spread it in such a way that that current rural water district customers would see their water bills cut in half. The average family of four who uses 6000 gallons per month now pays a water bill of \$60.00 plus tax each month. A \$360.00 yearly reduction in that family's water bills would be very substantial.

The district would also benefit from the the improved management level the City of Topeka has to offer. There are currently no full time employees, and no one to answer the phone during the day in this district.

Reduced water bills and full time active management would be huge benefits to the patrons of this district.

In conclusion, passage of house bill 2003 would allow this to occur. We ask for your favorable action on this bill. Thank you very much.

Submitted by: Gayle Bayless, Manager, Shawnee Co.  
Rural Water  
District #7

YMK  
1/23/2003

House Local Government

Date: 1-23-2003

Attachment # 5

Law Offices  
STUMBO, HANSON & HENDRICKS, LLP  
2887 S.W. MacVicar Avenue  
Topeka, Kansas 66611  
Telephone (785) 267-3410  
Telefax (785) 267-9516

Gary H. Hanson  
Larry D. Hendricks

Tom R. Barnes II  
Todd A. Luckman  
Wesley F. Smith

Walter G. Stumbo  
(1911 - 1998)

gary@stumbolaw.com

January 23, 2003

Representative Jene Vickrey  
Chairman, House Committee on  
Local Government

**Re: Testimony in Support of House Bill 2003**

Dear Chairman Vickrey and Members of the Committee:

Our firm represents RWD No. 7, Shawnee County, Kansas. We are testifying in support of HB 2003.

RWD No. 7 is a rural water district organized under K.S.A.82a-612 et seq. It serves approximately 170 farms and homes in southern Shawnee County.

The City of Topeka Water Department has proposed to acquire RWD No. 7. Under the proposed agreement, the City would assume responsibility for service to all of RWD No. 7's customers, take title to its assets, pay all of its debts, and provide for service to future customers. The governing body of the District supports the proposed agreement because it would result in a higher level of service to the District customers, while average monthly water bills would be reduced by approximately one-half. For these reasons, the District's board of directors expects that its customers would also support the agreement.

On behalf of the District, we requested an Attorney General's Opinion on the legality of the proposed agreement. The Attorney General's Opinion, dated June 25, 2002, is that although the transfer "may be quite sensible and in the parties best interests, it is my opinion that there is no statutory authority" for the transfer. (See, Attorney General's Opinion Letter attached.)

House Bill 2003 would provide this authority. It is modeled after K.S.A. 19-3512, a statute concerning Water Supply and Distribution Districts, under which Water District No. 1 in Johnson County has successfully annexed territory and acquired water systems on several occasions.

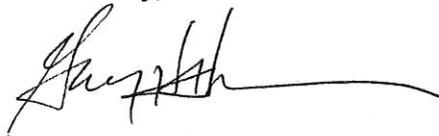
House Bill 2003 provides a tool by which a city could acquire the territory and facilities of a rural water district if the governing body of the city and of the water district agree. Protections are provided to the water district customers in that the agreement, along with a statement of the

House Local Government  
Date: 1-23-2003  
Attachment # 6

reasons therefor, must be mailed to all customers of the district, a copy of the agreement is filed in the office of the County Clerk of each county where the water district provides water service, and also published in the newspapers for the area. If a petition signed by at least 10% of the participating members (customers) of the water district requests an election on whether the agreement should take effect, then the agreement cannot take effect until that election is held and approved by a majority of the members.

As the case of RWD No. 7 and the City of Topeka shows, there are instances where considerable efficiency can be obtained by merging a small water system like RWD No. 7 into a larger one. In many instances, there is no way achieve this end under existing law. House Bill 2003 would provide a tool that water systems could use in realizing these efficiencies. We urge you to give your favorable support of HB 2003.

Sincerely,

A handwritten signature in black ink, appearing to read "Gary H. Hanson", with a long horizontal flourish extending to the right.

GARY H. HANSON

GHH:de



State of Kansas

## Office of the Attorney General

120 S.W. 10th Avenue, 2ND FLOOR, TOPEKA, KANSAS 66612-1597

CARLA J. STOVALL  
ATTORNEY GENERAL

June 25, 2002

MAIN PHONE: (785) 296-2215  
FAX: 296-6296

Gary Hanson  
Stumbo, Hanson & Hendricks  
2887 S.W. McVicar  
Topeka, Kansas 66611

Elsbeth Schafer  
Office of the City Attorney  
215 S.E. 7<sup>th</sup>  
Topeka, Kansas 66603

Re: Proposed Acquisition of RWD No. 7's Assets and Liabilities by the City of Topeka

Dear Gary and Beth:

After reviewing Gary's letter of June 18, it is my opinion that the Water District (District) has no express or implied authority to transfer all of its assets and liabilities to the City of Topeka.

As you know, the District is a creature of statute<sup>1</sup> and, therefore, can only do what the statutes expressly authorize it to do or by implication in order to "give effect to powers specifically granted."<sup>2</sup> The statutory authority upon which you rely is the District's ability to contract and hold real property.<sup>3</sup> The Attorney General opinion that you cited<sup>4</sup> sanctions the sale of District assets as an implied power that emanates from the express power to hold title. However, the opinion is limited to sales of property necessary "for the successful operation of the district." Your proposed transfer would divest the District of its ability to operate. Moreover, while the District has the authority to contract, I do not believe the Board of Directors has the authority to enter into a contract that will essentially emasculate the District.

---

<sup>1</sup>*Dedeke v. Rural Water Dist. No. 5 Leavenworth County*, 229 Kan. 242 (1981).

<sup>2</sup>Attorney General Opinion No. 2001-4; 87-19.

<sup>3</sup>K.S.A. 82a-619(a)(3)(4).

<sup>4</sup>Attorney General Opinion No. 87-146.

6-3

Gary Hanson  
Elsbeth Schafer  
Page 2

My opinion is buttressed by the fact that the District statutes set forth only two ways for a rural water district to cease operations, which, in effect, is what you propose: K.S.A. 82a-629 which provides for dissolution by the Board of County Commissioners and K.S.A. 82a-637 which, under certain conditions, provides for transfer of assets to a city of the first class.

While this transaction may be quite sensible and in the parties' best interests, it is my opinion that there is no statutory authority which would allow the Board of Directors to transfer all of the District's assets and liabilities to the City of Topeka.

Very truly yours,

OFFICE OF THE ATTORNEY GENERAL  
CARLA J. STOVALL



Mary Feighny  
Assistant Attorney General

MF:jm

JM SLOAN  
 REPRESENTATIVE, 45TH DISTRICT  
 DOUGLAS COUNTY

STATE CAPITOL BUILDING  
 ROOM 446-N  
 TOPEKA, KANSAS 66612-1504  
 (785) 296-7677  
 1-800-432-3924

772 HWY 40  
 LAWRENCE, KANSAS 66049-4174  
 (785) 841-1526  
 sloan@house.state.ks.us



TOPEKA

HOUSE OF  
 REPRESENTATIVES

COMMITTEE ASSIGNMENT  
 CHAIRMAN: HIGHER EDUCATION  
 MEMBER: UTILITIES  
 ENVIRONMENT  
 GENERAL GOVERNMENT &  
 HUMAN RESOURCES  
 BUDGET

## TESTIMONY ON HB 2011 – LOCAL GOVERNMENT COMMITTEE

Thank you, Mr. Chairman. Members of the Committee, I am chairman of Douglas County Rural Water District #1. The District is not a taxing authority; our revenues are derived from the sale of drinking water and benefit units, and from earnings on the investment of our idle funds. We have funds invested through four financial institutions and our financial advisors at each institution regularly bring us investment options for us to consider. Alternative investment options, with potentially higher rates of return, are important to our Board members as we work to avoid increasing water rates to pay for higher operating costs.

HB 2011 is the result of one of those conversations with our “personal” financial advisor at one of Lawrence’s financial institutions. There are two components to HB 2011. First, is that equity-linked certificates of deposit are authorized as an investment option. Equity-linked CDs will be explained in greater detail by other conferees, but the key point for my Board members is that the return of the principal invested is guaranteed (pg. 4, lines 16-17), though the rate of return is variable. While my fellow Board members are willing to assume some risk on the rate of return (current conventional CDs, money market accounts, and savings accounts provide returns of approximately 2 percent or less), we are not willing to risk the principal.

The second component of HB 2011 is to extend the time for which municipalities may invest idle funds from two to five years. The extension of time is the minimum necessary today to purchase equity-linked CDs.

HB 2011 seeks to provide local officials with another idle funds investment option. Equity-linked certificates of deposit are optional, risk-free for the principal, and hold the potential to earn local governments a higher rate of return than do currently available investment options. I recognize that not every Board will want to utilize this investment option, and that is as it should be. There are options available to my water district today that are not appropriate for us because of the length of investment, projected rate of return, amount of investment required, or other considerations.

Please note on page 4, line 16 the language “approved by the state bank commissioner.” In a conversation with the State Banking Commissioner Franklin Nelson, Mr. Nelson believes that it is inappropriate for his office to assume such a role because the Commissioner does not believe that it is appropriate to review every investment

House Local Government  
 Date: 1-23-2003  
 Attachment # 7

opportunity available through every financial institution. That was never my intention and I agree that the language in quotes above should be deleted from the bill.

Mr. Nelson stated during our conversation that if the language is deleted, he has “No problem with the bill.”

I encourage you to recommend HB 2011, with the suggested deletion, favorably for passage so that local governments will have another tool to wisely invest their idle funds for the ultimate benefit of their – and our – constituents.

Post Script Thoughts: As part of my due diligence, I spoke with a representative of the Pooled Money Investment Board about equity-linked certificates of deposit and HB 2011. That person expressed reservations about local officials being capable and knowledgeable enough to wisely determine whether equity-linked CDs are an appropriate investment. There was an implication that the state needed to protect local officials from themselves. As one of those local officials, I was mildly offended. We are selected to represent our neighbors, work with reputable members of the Kansas financial community, and make decisions about how to best manage our, and their, financial and other resources. As I indicated above, we currently manage investments through four local financial institutions, we are wise stewards of our patron’s money.

It was noted that equity-linked CD funds would be insured only up to the \$100,000 threshold, there is a penalty for early withdrawal, etc. Most of these “limitations” are similar to the situation with other permitted investments. Equity-linked certificates of deposit are not for every municipality. But then neither are savings accounts.

Questions were also raised about local governments facing liquidity problems with a five year investment. Again, local officials, working with their financial advisors, are not going to tie-up all of their idle funds for five years. In addition to local financial institutions, the League of Kansas Municipalities, Kansas Rural Water Association, Kansas Association of Counties, and other statewide organizations also provide counsel to local governments. But, if the Committee prefers to extend the investment period from two to five years only for equity-linked CDs, that is acceptable. Similarly, if the Committee wants to cap investments in equity-linked CDs at 20 percent of the local government’s idle funds, that also is fine.

Equity-linked certificates of deposit and HB 2011 are not a “threat” to the Pooled Money Investment Board. I simply ask Committee members to give local officials another tool with which to manage their responsibilities on behalf of the citizens of Kansas.



THE TRUST COMPANY  
OF KANSAS

3120 MESA WAY, SUITE B

P.O. BOX 442288

LAWRENCE, KANSAS 66044-8935

785-749-0904

800-749-0904

FAX 785-749-2388

www.tckansas.com

## HB 2011 Testimony

By:

Janis C. Bunker, CTFA  
Senior Vice President & Trust Officer  
The Trust Company of Kansas

President  
Kansas Bankers Association Trust Division

As a trust company chartered by the Kansas Bank Commission, we continually work with the statutes governing a trustee or fiduciary.

Local government officials also have a fiduciary obligation to their constituents. It is appropriate that they seek the highest possible return for public funds while safeguarding the principal amounts with which they are entrusted.

The Kansas Prudent Investor statute requires a fiduciary to diversify an investment portfolio.

The Kansas Prudent Investor statute also requires a fiduciary to guard an investment portfolio against inflation. This can only be done with exposure to equities.

An equity linked CD allows local government to fulfill both of these expectations.

Equity linked certificates of deposit would give local government organizations the ability to enjoy the growth found in equity investments with no exposure to loss for their principal.

When local government purchases an equity linked CD at their local bank, it also benefits that bank since the money remains in the community. This is a win-win situation.

We live and pay taxes in the Kansas communities affected by local government. We make this recommendation because we are trying to do what is best for local government.

House Local Government  
Date: 1-23-2003  
Attachment # 8

PROVIDING TRUST SERVICES IN  
THESE KANSAS COMMUNITIES

WICHITA  
LAWRENCE  
LEAVENWORTH  
ARKANSAS CITY  
ATCHISON  
AUGUSTA  
EMPORIA  
EUREKA  
EVEREST  
HARPER  
HAVEN  
OLPE

CHARTER MEMBER OF ASSOCIATION  
OF INDEPENDENT TRUST COMPANIES

*Serving the finest families in Kansas*

Kansas Legislative Committee Comments  
HB 2011 Testimony

Craig Jordan  
President, Index Powered CD (IPCD)  
Index Powered Financial Services, LLC  
Denver, CO

I represent Index Powered Financial Services, LLC (IPFS), a financial services company that has provided services and products to community financial institutions for over 20 years. Today's discussion will center on an explanation of equity linked certificates of deposit. These deposit products differ from traditional CDs primarily in the fact that their return is not a "fixed interest" return, but a "variable interest" return based on the appreciation of a stock index (i.e. S&P, Nasdaq, Dow, Russell) over a certain period of time. Equity linked CDs have been offered through large financial institutions such as Chase, JP Morgan, Bank of America and LaSalle Bank since the mid-1980s.

During the economic boom of the 1990's, investment in stocks/equities by both individual investors and mutual fund managers resulted in a critical liquidity problem for the nation's community banks through the diversion of funds that traditionally were deposited in the financial institutions. Deposits are the life-blood of community banks - they fund loan demand and community development needed to create a growing and vibrant market. To help stem this tide, our company devised a plan to develop equity linked CD products for the community banker. The program was designed with IPFS offering support and a stock index license to sell the product, the Federal Home Loan Bank of Topeka offering an option contract to the community bank to reduce risk, and of course, the community banks offering the CD product to their customers. Our goal was to provide an additional product the community bank could offer to compete with brokers, mutual funds and even insurance companies for deposits. These financial competitors are continuously devising plans to gather and control larger percentages of the finite amount of deposits available in the market. During the last two years, we have had over thirty banks in Kansas, as well as other community banks in fifteen other states, offering equity linked CDs to their customers and to other financial institutions. Kansas banks have received authority to offer equity linked CDs from the State Bank Commissioner, the Honorable Franklin W. Nelson. In addition, the Federal Deposit Insurance Corporation (FDIC) has opined that equity linked CDs are eligible for deposit insurance.

The equity linked CD product offered through Kansas bankers is structured as follows:

- 5-year term CD
- FDIC insured deposit
- Principal invested is guaranteed if the CD is held to maturity - principal protection
- Interest return is based on the appreciation of the S&P 500 index - no guarantee, no limit
- No fees to the investor

The ability to offer the equity linked CD product to local municipal or other public units by Kansas community banks could provide a conduit to maintain additional local funds in the community. The additional source of funds deposited in the community bank for the 5-year period of time assists bankers in meeting the needs of the community while offering the public unit additional investment opportunities.

House Local Government  
Date: 1-23-2003  
Attachment # 9

**Equity-Linked Certificates of Deposit  
An Investment Alternative for Kansas Municipalities**

**Facts and Concerns**

1. This product is currently being marketed (by Risk Analytics Inc.) to commercial banks as a retail product.

**Response:** Index Powered Financial Services, LLC (previously known as Risk Analytics, Inc.), in collaboration with the Federal Home Loan Bank of Topeka, has developed an equity-linked CD product. This product is available through participating Kansas community financial institutions for retail customers and it is also being purchased by many of these institutions for their own investment portfolios. In addition, all products offered by banks are considered retail products. This should not preclude the use of such products by municipalities.

2. The product has only been in existence for 24 months.

**Response:** The Index Powered Financial Services, LLC. (IPFS) product has been offered monthly since February, 2001. It is currently the only equity linked CD product offered on a continuous basis by community based financial institutions. Equity Linked CDs have been in existence since the mid-1980s and offered periodically by large money center banks.

3. To date they have only one government entity as a client.

**Response:** True statement. There has simply not been any concerted effort to market the product to governmental entities by participating institutions primarily due to a similar time limitation imposed by statute.

4. The only maturity available at this time (through RAI) is 5 years. (This opens up the opportunity of chasing yields at the expense of matching cash flows.)

**Response:** The 5 year term was deliberately selected to avoid "chasing yields" – time in the market, rather than timing the market. Further, a review of the historical performance of the S&P 500 indicates that any equity linked CD issued after February of 1974 (assuming the product existed at that time) would have paid some rate of return, in addition to the original principal investment. The only risk is the opportunity cost of an alternative fixed rate instrument.

5. There is no annual cash flow from these investments. (All interest earnings, if any are paid at maturity).

**Response: True statement. The equity linked CD is intended for those able to hold the investment for the full 5 year period. It is not intended to meet short term liquidity needs.**

6. There is really no secondary market for these certificates should you need the cash prior to maturity.

**Response: Bank CDs are not negotiable instruments. This is a bank issued certificate of deposit, just like any other CD. It is not a DTC tradable instrument; it does not have a CUSIP number. There is a redemption provision, however, should funds be needed and there is the option to use the CD as collateral for a loan with the issuing institution.**

7. There are early withdrawal options, but then principal is not guaranteed. Principal may be lost based on the "Market Measure Calculation."

**Response: Early redemption is based upon the "Market Measure Calculation" provided by the Federal Home Loan Bank. However, it is not necessarily the case that principal will be lost, it is simply a possibility. This is no different than any other bank issued Certificate of Deposit with an early withdrawal penalty provision. Again, it is not recommended as an investment option to meet short term liquidity needs.**

8. They are FDIC insured up to \$100,000. Any amount in excess of this is the promise of the issuer. Federal Home Loan Bank letters of credit or surety bonds can be provided for this excess however this will reduce the return.

**Response: Incorrect statement. Any expense to cover excess FDIC insurance (a letter of credit or surety bond) is an expense borne by the financial institution. There is absolutely no impact to the return paid the customer.**

9. Even if principal is adequately protected, municipalities could end up with a five-year investment with no return.

**Response: True statement. However, for this to occur the stock market/S&P 500 would have to remain stagnant or lose value for the entire five year period. The unknown is the upside potential versus no return.**

10. While they are touted as a product with no management or sales fees the fact that there are several parties involved in the transaction most likely negatively impact the ultimate return.

**Response: Incorrect statement. There are absolutely no fees or charges that accrue to the CD customer. The return is based upon a well defined calculation, and any**

**resulting return is paid directly to the customer based on that calculation at maturity. There are no deductions.**

11. There really is no benchmark for comparison to this product. You are put in the position of speculating on the direction of the S&P 500 over the next 5 years.

**Response: The S&P 500 is considered the standard for measuring large company stock market performance and is used as the yardstick for comparison by mutual fund companies. It has been in existence since 1923. Again, any equity linked CD issued since February of 1974 would have realized a positive return. The average 5 year return for the S&P 500 for the period of late 1935 to late 2001 is 7.69%. The equity linked CD return (had it been in existence for the same period) is 5.52%.**

12. These Equity-Linked Certificates of Deposit have not been recommended by any federal or state securities commission or regulatory authority nor are they registered under the Securities Act of 1933.

**Response: Certificates of Deposit are already approved investment instruments. Equity linked certificates of deposit are the same as any other bank offered CD with three notable exceptions: the interest calculation method, timing of the interest payment (at maturity), and early withdrawal provision. Further, federal and state regulatory authorities do not recommend investment products – they approve or disapprove them for sale within their respective area of jurisdiction. The equity linked CD has, indeed, been approved for offering by community financial institutions by the FDIC and various state banking authorities (including Kansas).**

**It is not required that an equity linked CD be registered under the Securities Act of 1933. It is not a security – it is simply a bank certificate of deposit, and as such it does not fall under the referenced act.**

13. Providing this as an investment alternative to all cities, counties, school districts, rural water districts, fire districts, community colleges, etc. in the state of Kansas would be a significant departure from the risk characteristics of the current investment options. (U.S. treasuries, Kansas bank CD's and the Kansas Municipal Investment Pool). The varying levels of financial expertise within each municipality compound this risk.

**Response: As indicated in this concern, local governmental entities *already* use “Kansas bank CD's” as an investment option. The equity linked CD differs only in the interest calculation method, timing of the interest payment and early withdrawal provision. Use of an equity linked CD product also serves as a hedge against inflationary pressures.**

**However, this product is not being suggested as total replacement for current investment options. It is simply being offered as another alternative and as a way to realize some upside potential earnings growth. Because the equity linked CD is offered by community financial institutions, each dollar invested remains in the community to further foster economic growth through agricultural, business, automobile and home loans.**

HB 2011 Testimony

Eric Donaldson  
Assistant Vice President and Controller  
Silver Lake Bank  
Topeka, KS

In order to maintain our bank's core deposits we recognized the need to seek alternative investment options for our banking customers. After due consideration, we elected to offer an equity linked certificate of deposit product. It offered the best of both worlds for our customer base – principal protection through FDIC insurance and the ability to realize greater investment growth than a traditional CD because of linkage to a market index. We have actively promoted this product since September of 2001 to customers previously reluctant to invest in the stock market and to those sophisticated investors who finally could take advantage of a competitive product from their hometown bank. Our results have been very positive – both from the bank's perspective as well as the customer's.

From the institutional perspective, offering such a product has allowed us to meet a customer need for longer term financial planning - as well as realize growth in the bank's mid to longer term core deposits. As a consequence, our bank is better able to offer longer term asset products - loans for businesses, homes, automobiles, etc. The customer's dollar remains in the community and is reinvested in the community.

HB 2011 would further support the growth of critically needed longer term core deposits in Kansas community financial institutions. Permitting local governmental units to invest funds within their local communities for a longer period of time improves the health of those financial institutions and the community at large. This change clearly supports the admirable goal of community reinvestment. It would also support financial strategic planning for the governmental body – money that could be ear-marked for capital improvements – with the opportunity for unlimited upside growth, but without risk to the principal investment. In our opinion, HB 2011 opens new avenues for local governmental entities, Kansas financial institutions and Kansas communities.

House Local Government  
Date: 1-23-2003  
Attachment # 10

Comments on House Bill 2011  
Before the House Local Government Committee  
Thursday, January 23, 2003

Mr. Chairman and Members of the Committee:

My name is John J. Haas, President of Ranson Financial Consultants, LLC, Wichita, Kansas. The Ranson family of companies has been providing financial advisory services to local units of government in Kansas since the 1930's. I have been with Ranson since 1984, except for a two year period when I was an investment advisor for Edward D. Jones & Company, LLP. Ranson also acts as the financial advisor to the Kansas Rural Water Finance Authority. Even though we do not offer professional investment advice to our clients, we often provide direction, with the assistance of qualified bond counsel, regarding the statutory parameters for the investment of public funds. I appreciate the opportunity to comment today in support of HB 2011 with certain amendments.

Last week we sent a survey to about 20 of our clients to get their response in regard to HB 2011. We received six responses to the survey; generally, all were in favor of HB 2011. The primary change that we are in support of is increasing the investment period in a Certificate of Deposit ("CD") from two to five years. As with any investor, local units of government need to be able to match the investment horizon with its cash requirements. Many local units of government would rather save its money over a period a time, rather than to go into debt, to pay for one or more future capital projects. Having the option to obtain a CD with a five-year investment life gives local units of government the opportunity to better plan for these long-range capital expenditures. Local units of government can often receive a higher rate of return since it can be invested for a longer period of time, too.

Ranson has one client who has requested that the bill be amended to allow local units of government to purchase CD's from local credit unions. Smaller local units of government usually have very limited investment options. As credit unions become more pervasive across the State of Kansas it gives smaller local units of government one more option for the investment of idle funds. We would recommend that local units of government be allowed to invest with local credit unions since the NUCA is similar to the FDIC.

Our single major concern about HB 2011 is allowing local units of government to invest in equity-linked certificates of deposit. For many years Kansas has received high marks from the nationally recognized rating agencies for its conservatism. Non-rated debt of almost every Kansas municipality will trade at about the "A" rating level because of the recognition of our conservatism. In the field of investing there is a direct correlation between potential risk and rate of return. With an equity-linked CD there is a guarantee that the holder will receive a 100% return of principal, if held to maturity. I beg to ask who is taking the risk if the value of the equity-linked CD goes down over the investment period. It is certainly not the FDIC. It insures deposits from bank defaults, not market losses.

House Local Government

Date: 1-23-2003

Attachment # 11

From the prospectus provided to me by a Kansas banking institution on one of these types of investments an equity-linked CD will pay-out 90% of the return on investment based upon the Standard and Poor's 500 index. This means that someone is taking a 10% risk premium to insure that the investment will not go down over the investment horizon. If the value of the investment goes down, somebody loses. What if this risk taker is unable to cover the losses at the end of investment horizon? The prospectus states that the website for information on this investment is "owned and operated by Index Powered Financial Services, LLC ("IPFS"), a Colorado limited liability company. Where are these investments really coming from? What if the local bank has gotten in over its head regarding what it thought was a no-loss situation? In an attempt to obtain a higher rate of return on investment many smart public officials in Orange County, California, must have thought the same thing. FDIC and pledged securities would ultimately cover the losses. But do we want local units of government in Kansas to be involved in something that could create problems for the State's banking system?

Other items of concern with equity-linked CD's include early withdrawal, unless under the event of death of the holder, is prohibited except on the anniversary date and the principal is subject to market valuations in event of early withdrawal. This would mean local units of government could not remove money from the CD in the event of an emergency except on the anniversary date and there could be significant market risk if it decided to do so. This would significantly reduce the liquidity of the investment.

In summary, we would like to see the bill passed with amendments adding credit unions as an authorized investment provider and the removal of equity-linked CD's as an authorized investment.

Respectively submitted,

John J. Haas, President  
Ranson Financial Consultants, LLC



**POOLED MONEY INVESTMENT BOARD**

Landon State Office Building  
900 S. W. Jackson Street  
Suite 209  
Topeka, KS 66612-1220

Ph. (785) 296-3701  
Fax (785) 296-1085

<http://kansasstatetreasurer.com/pmib>

DIRECTOR OF INVESTMENTS  
Derl S. Treff

**TESTIMONY ON HOUSE BILL 2011**

by

Derl S. Treff

Director of Investments

Pooled Money Investment Board

January 23, 2003

The Honorable Jene Vickrey  
House Committee on Local Government  
Statehouse, Room 115-S  
Topeka, Kansas 66612

Representative Vickrey and Members of the Committee:

*Subject: Inclusion of Equity-Linked Certificates of Deposit as an investment option for Municipalities*

This type of product would significantly increase the risk level of a municipality's investment portfolio. This product appears to be marketed as a retail product rather than a product for governmental or other institutional investors. This is a relatively new investment product and we have found little support for it among governmental or other institutional investors. The only maturity available is 5 years. This product is by definition a derivative instrument, in that the value of the investment is determined by price movements in a stock index. (In this instance the S&P 500).

There is no annual cash flow from these investments, as all interest earnings, if any, are paid at maturity. Should the funds be needed prior to maturity there is really no secondary market and even though there is FDIC insurance coverage up to \$100,000 should you initiate an early withdrawal option, the principal is not guaranteed.

There really is no benchmark for comparison to this product. Municipalities would be put in the position of speculating on the direction of the S&P 500 over the next 5 years. No

House Local Government

Date: 1-23-2003

Attachment # 12

other investment currently available to municipalities requires this type of speculation to estimate its return.

Providing this as an investment alternative to all cities, counties, school districts, rural water associations, fire districts, community colleges etc. in the state of Kansas would be a significant departure from the risk characteristics of the current investment options (U.S. treasuries, Kansas bank CD's and the Kansas Municipal Investment Pool). The varying levels of financial expertise within each municipality compound this risk.

I wish that I had some other investments to suggest that could help municipalities improve their investment earnings. However, because of the almost unprecedented level of interest rates (lowest in over forty years) and the weak fiscal condition of most government entities, this is not the time to take additional risk with taxpayers' money by raising the risk tolerance of portfolios and/or "chasing yield" by investing in longer maturities.