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November 18, 2013

ATTORNEY GENERAL OPINION NO. 2013-18

Todd Luckman, City Attorney  
City of Auburn  
2887 SW MacVicar Ave.  
Topeka, KS 66611

Re: Bonds and Warrants—Cash-Basis Law—Limits of Indebtedness

Synopsis: For purposes of the cash-basis law, the term “indebtedness” refers only to financial obligations that are binding, not those that are contingent on future events. As applied to a ten year contract for the wholesale purchase of natural gas that may be terminated with three years’ notice, any expenses beyond the three year period are contingent on the city not cancelling the contract and therefore do not constitute an indebtedness of the city. Cited herein: K.S.A. 10-1101, 10-1113, K.S.A. 2013 Supp. 10-1116.

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Dear Mr. Luckman:

As the City Attorney for the City of Auburn, you ask whether a proposed contract for the wholesale purchase of natural gas would violate the cash-basis law.<sup>1</sup> This law generally prohibits municipalities from incurring indebtedness in excess of the amount of funds they have on hand, unless one of the exceptions to the law applies.<sup>2</sup> As relevant here, the law contains a specific rule for municipal enterprise funds set up for the financing of municipal utility services. For these funds, the limit of indebtedness is “100% of the accrued revenue of the current fiscal year plus any balances carried forward, cash reserves, intergovernmental grants, and sums advanced to qualify for intergovernmental grants.”<sup>3</sup>

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<sup>1</sup> K.S.A. 10-1101 *et seq.*

<sup>2</sup> K.S.A. 10-1113.

<sup>3</sup> K.S.A. 2013 Supp. 10-1116(b)(2).

You explain that the City of Auburn purchases natural gas at wholesale from an entity called the National Public Gas Agency (NPGA) and operates a utility that resells this natural gas to city residents. The standard NPGA contract lasts for ten years and is automatically renewed every year, restarting the ten year period.<sup>4</sup> The standard contract may be terminated by either party with three years' notice, but because of concerns about the cash-basis law, the city has modified the standard contract to allow the city to terminate the contract at any time due to insufficient funds. As a result of this modification, NPGA charges the city additional fees that it would not charge under the standard contract.

You wish to know whether the standard contract, without the existing modification, would satisfy the requirements of the cash-basis law. You inform us that the city has enough money on hand to cover the cost of natural gas service for three years, but not enough to cover the entire ten year period. Thus, your question boils down to whether the city's "indebtedness" for purposes of the cash-basis law would be the city's obligations under the entire ten year contract or only the city's obligations for the three year period during which the city would be required to pay for natural gas in the event of a cancellation.

Attorney General Opinion No. 98-13 discussed the meaning of the term "indebtedness" as used in the cash-basis law and concluded that the term refers only to financial obligations that are binding, not those that are contingent on future events.<sup>5</sup> The opinion based its analysis, in part, on the Kansas Supreme Court's decision in *City of Wichita v. Wyman*,<sup>6</sup> which held that the City of Wichita could act as a self-insurer for workers' compensation purposes without having enough money on hand to cover all potential future claims. The Court reasoned that such an arrangement would not violate the cash-basis law because "until an award and judgment to pay compensation to an injured workman are assessed against the city, its liability is only contingent, not absolute."<sup>7</sup>

Attorney General Opinion No. 98-13 considered a proposed agreement that would have required a county to make annual payments over the course of forty years into a trust fund set up for the care of the county landfill. Even though the payments were not due until future dates, the opinion concluded that the entire forty year sum constituted indebtedness for purposes of the cash-basis law because the payments were not dependent on any contingency but would become an unconditional, binding obligation once the agreement was executed. Thus, whether an expense constitutes indebtedness does not depend on when payment is due. Instead, the key distinction is whether the obligation is contingent on future events or binding and certain to occur.

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<sup>4</sup> We are not offering an interpretation of the terms of the contract. This opinion is based on the facts as stated in your request letter.

<sup>5</sup> See also Attorney General Opinion No. 2007-25 (same).

<sup>6</sup> 158 Kan. 709 (1944).

<sup>7</sup> *Id.* at 713; see also *Int'l Ass'n of Firefighters v. City of Lawrence*, 14 Kan. App. 2d 788, 799-802 (1990).

Todd Luckman  
Page 3

Under the standard natural gas contract you describe, the City of Auburn would only be bound to pay for three years' worth of natural gas supply at any given time. Because the obligation to pay any expenses beyond this three year period would be contingent on the city not cancelling the contract, those expenses would not constitute an indebtedness of the city for purposes of the cash-basis law.

Sincerely,

Derek Schmidt  
Attorney General

Dwight Carswell  
Assistant Attorney General

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