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The Senate of the State of Texas

Jane Nelson
Senate District 12

August 12, 2015

RQ-0045-KP

Honorable Ken Paxton
Office of the Attorney General
Attention: Opinion Committee
P.O. Box 12548
Austin, Texas 78711-2548

Re: Request for opinion regarding the validity of a contract between political subdivisions of the State of Texas

Dear Attorney General Paxton:

Pursuant to Section 402.042 of the Texas Government Code, please accept this letter as a request for an opinion on whether a contract between two political subdivisions of the State of Texas may assign the right of one such political subdivision to (1) approve annual budgets for operating facilities necessary to provide services to the residents within its boundaries; (2) issue building permits for construction within its boundaries; (3) contract for security and emergency medical services within its boundaries; and (4) convey, assign, commit or otherwise reserve unused capacity in its facilities to the other political subdivision to undertake on its behalf.

FACTUAL BACKGROUND

At issue is an agreement entered into by and between Denton County Fresh Water Supply District No. 1-A ("1A") and Denton County Fresh Water Supply District No. 1-B ("1B") to provide for the operation and maintenance of water and sewer facilities within their respective boundaries (the "Operating Agreement"). A copy of the Operating Agreement is attached hereto for reference. 1A and 1B are each political subdivisions of the State of Texas, created and organized pursuant to Article XVI, Section 59 and Article III, Section 52 of the Texas Constitution (1A and 1B sometimes referred herein collectively as the "Districts").

At an election held within what was to become the Districts on January 17, 1983, voters approved the creation of Denton County Fresh Water Supply District No. 1 (the "Original District"). As created, the Original District operated under the provisions of Chapter 53, Texas Water Code, as amended. Subsequently, the Original District converted to a water control and improvement district, operating under the provisions of Chapter 51, Texas Water Code, as amended. Chapter 49, Texas Water Code, as amended, also applied to the Original District, as well as the Districts (Chapters 49 and 51 referred to herein as the "Code"). Finally, at an election held within the Original District on May 6, 1995, the Original District was divided into 1A and 1B.

The Districts provide water and sewer service via agreements with the Upper Trinity River Authority (the "Authority") and the City of Lewisville, Texas (the "City"), respectively. In concert with these agreements, the Districts entered into the Operating Agreement to provide for the orderly operation and maintenance of the water and sewer facilities within the Districts (the "District Facilities"). The Operating Agreement confers

operational responsibility upon 1A. The Operating Agreement, and this operational responsibility, has led to continuing disputes between the Districts.

DISCUSSION

The primary concern with the Operating Agreement is whether 1B contracted away certain of its legislative functions. Generally, governmental entities, such as the Districts, “[cannot], by contract or otherwise, bind [themselves] in such a way as to restrict...free exercise of...governmental powers, nor could [they] abdicate [their] governmental functions, even for a ‘reasonable time.’” *Clear Lake City Water Authority v. Clear Lake Util.*, 549 S.W.2d 385, 391 (Tex. 1977). Accordingly, 1B cannot “transfer control of its governmental functions to another entity, absent specific constitutional authorization.” *Pittman v. Amarillo*, 598, S.W.2d 941, 945 (Tex. Civ. App. Amarillo 1980, writ ref’d n.r.e.). See also Tex. Att’y Gen. Op. No. JC-0377 (2001). It does not follow, however, that 1B could not enter into a contract to fulfill its obligations to the public. *San Antonio River Auth. v. Shepperd*, 299 S.W.2d 920, 926-27 (Tex. 1957). Such an agreement is unlawful, however, if it has the effect of potentially controlling and embarrassing a governmental entity in the exercise of its governmental powers. *Clear Lake City Water Auth.*, 549 S.W.2d at 392. With this in mind, please consider the following provisions of the Operating Agreement:

1. Section 2.2 – 2.5 – Facilities Operating and Maintenance Budget.

Section 2.2 of the Operating Agreement establishes the Facilities Operating and Maintenance Budget (the “FOMB”), as well as the procedures for adopting, implementing and amending the FOMB. The FOMB covers all maintenance and operating expenses concerning the District Facilities. This section provides that 1A will prepare the FOMB and submit it to 1B for review. While this action appears innocuous at first glance, the Section provides that, if the total actual expenses incurred on behalf of 1B during the fiscal year do not exceed the estimated FOMB for that fiscal year by more than 12 percent, any and all comments made by 1B to the draft FOMB are deemed advisory only, and 1B is bound by the proposed FOMB, and therefore obligated to make the prescribed payments to 1A set forth therein. 1A only has to seek 1B’s express approval of the FOMB in the event the actual costs for the prior fiscal year exceed 12 percent of the FOMB.

Further, Section 2.4 provides that the FOMB constitutes authorization for 1A to pay all operation and maintenance expenses of the Facilities set forth in the FOMB without any actual approval from 1B if the 12 percent threshold is not exceeded. If 1A undertakes an expenditure considered to be an emergency, it is authorized to make such expenditures without approval by 1B. Finally, Section 2.5 provides that by its execution of the Operating Agreement, 1B approved the FOMB for the initial year of same. By these terms, so long as the actual costs never exceed 12 percent, 1B will never have the opportunity to expressly approve an FOMB throughout the term of the Operating Agreement.

Water control and improvement districts, such as the Districts, as well as other political subdivisions of the State created pursuant to Article XVI, Section 59, Texas Constitution, have been held, “in discharging their governmental functions, to be agents of the State, and are essentially exercising the State’s police power, being a grant of authority from the people to their governmental agents for the protection of the health, the safety, the comfort and the welfare of the public.” *Banker v. Jefferson County Water Control and Improvement District No. One*, 277 S.W.2d 130, 133 (Tex. Civ. App. – Beaumont 1955, writ ref’d n.r.e.). Certainly, budgeting for the maintenance and operation of facilities serving the public, and in turn ensuring that the public funds it is entrusted with protecting and expending responsibly, is a function of this police power to be properly exercised by 1B. These provisions could potentially abdicate 1B’s governmental duty, and embarrass 1B in the exercise of its budgeting duties.

2. Article 3 – Operation and Maintenance Services.

Article 3 of the Operating Agreement enumerates the terms by which 1A provides operation and maintenance services to 1B. This Article authorizes 1A to, among other things, (i) arrange for, supervise, enter into contracts and make expenditures for all aspects of the operation and maintenance of the Facilities; (ii) enter into contracts for professional services necessary for the operation and maintenance of the Facilities in accordance with the FOMB; (iii) negotiate with utility companies; (iv) coordinate with other entities; and (v) establish rates to be recommended to 1B; (vi) issue building permits within 1B. Most concerning of the aforementioned services is item (vi), the power to issue building permits. Under the terms of the Operating Agreement, 1A, as operator of the Facilities, has the authority to issue permits within 1B, which ordinarily would be a function of 1B's legislative authority.

3. Article 4 – Services and Payments.

Article 4 specifies the authorized services provided by 1A to 1B. These services include management, as well as billing to and collection from 1B residents for water and sewer services. Additionally, there are certain "miscellaneous" services detailed in this Article of the Operating Agreement. Such services include street lighting and, more importantly, police and emergency services. The Operating Agreement states that 1A shall contract with the City for the provision of police and emergency services, and 1B shall be responsible for its share of the costs thereof. Pursuant to Section 49.216 of the Code, 1B has the power to contract for the services of peace officers with the power to make arrests to prevent or abate the commission of any offense against the rules of the District or the laws of the State of Texas. While nothing in the Operating Agreement states that 1B cannot enter into other contracts for security services, it would still be obligated to utilize and expend its funds for the City services. Effectively, this provision removes 1B's right to, among other things, decide whether to (i) enter into such an agreement with the City for said services, or (ii) to continue such an agreement in effect if, for whatever reason, 1B decides it is unhappy with the City services. This is a core governmental function of 1B that is potentially removed from its purview by the terms of the Operating Agreement.

4. Article 5 – Approvals and Capacity.

Article 4 of the Operating Agreement stipulates that (i) 1A may take any actions reasonably contemplated and required by the approval of the FOMB without any prior approval by 1B; and (ii) that 1B will not transfer, assign, or convey any of the unutilized capacity, if any, in the District Facilities which have been financed by 1B to any party other than 1A or an entity approved by 1A, on terms and conditions decided upon by 1A. Item (i) above is concerning, as previously discussed, because 1B only has the ability to approve the FOMB if it meets the 12 percent threshold. Otherwise, 1B has no authority to approve the expenditures covered by this Section. Moreover, item (ii) removes 1B's authority to contract for or otherwise utilize its unused capacity; except by way of approval by 1A. The Districts almost certainly have differing, and potentially conflicting, motives when it comes to unused capacity. Given this provision, 1B cannot make a commitment or contract for a reservation of its own capacity without first allowing 1A to weigh in. 1A stands in the place, and could frustrate 1B in the exercise of its judgment concerning its unused capacity, for which its residents have paid, or continue to pay. Certainly, this is a governmental function. In fact, the Court in *Clear Lake City Water Auth.* expressly stated that "the determination of whether, on any particular date, it is in the best interests of all of its customers and the public in general, to extend water and sewer service to a particular person or entity" is a governmental function. 549 S.W.2d at 392.

Notwithstanding the concerns outlined above, Section 49.213 of the Code provides that a district may enter into contracts, which may be of unlimited duration, with persons, or any public or private entity, for, among other things, (i) the maintenance and operation of any works, improvements, facilities, plants, equipment, and appliances of the district or of another person or public or private entity; and (ii) the exercise of any other rights, powers and duties granted to a district.

Considering the legal authority cited above, namely the general principle that a governmental entity cannot enter into agreements that transfer its governmental functions to another entity, absent specific legislative authority, and Section 49.213 of the Code, which allows a district to enter into contracts for the exercise of its rights, powers and duties, I respectfully request your opinion on whether or not the Operating Agreement, particularly the provisions enumerated in this letter, constitutes an impermissible abdication of 1B's governmental functions. Moreover, if Section 49.213 of the Code does allow such an agreement, do the enumerated provisions exceed the authority to so contract granted by the Code?

Thank you for your assistance with this matter, and please do not hesitate to contact my office if you or your staff have any questions.

Very truly yours,

A handwritten signature in black ink that reads "Jane Nelson". The signature is written in a cursive, flowing style.

Senator Jane Nelson