

No. 09-20-00180-CV

**Ninth Court of Appeals
Beaumont, Texas**

SAN JACINTO RIVER AUTHORITY,

Appellant,

v.

CITY OF CONROE, TEXAS, AND CITY OF MAGNOLIA, TEXAS

Appellees.

*On Appeal from the
284th Judicial District Court, Montgomery County, Texas
Cause No. 19-09-12611*

BRIEF OF AMICUS CURIAE IN SUPPORT OF APPELLANT

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November 13, 2020

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BRIEF OF AMICUS CURIAE IN SUPPORT OF APPELLANT

TO THE HONORABLE NINTH COURT OF APPEALS:

Northeast Texas Municipal Water District (“NETMWD”) submits this brief supporting the appeal to the Ninth Court of Appeals by the San Jacinto River Authority (“SJRA”) to overturn the 284th Montgomery County District Court’s ruling that wholesale water contracts between SJRA and the Cities of Conroe and Magnolia, Texas, were not subject to the legislature’s waiver of sovereign immunity for goods and services contracts. If allowed to stand, the District Court’s ruling to grant the Cities’ pleas to the jurisdiction in this matter will undermine long-term state and regional water supply planning efforts in Texas and the relevant public financing required for those efforts that is based on wholesale contracts between

governmental entities. NETMWD respectfully urges the Court of Appeals to overrule the District Court in the above-referenced matter and thereby affirm the importance of the legislature's broad waiver of governmental immunity for goods and services contracts, including wholesale water contracts generating revenue to secure public securities.

NETMWD adopts the Statement of the Case, Issues Presented, and Statement of Facts offered by Appellant SJRA.

STATEMENT OF INTEREST

NETMWD is a conservation and reclamation district created in 1953 under Article XVI, Section 59 of the Texas Constitution and operates in much the same way as Appellant SJRA. NETMWD is governed by a board of directors appointed by the city councils of the seven member cities that founded the District. To support its water supply obligations, NETMWD relies on revenue bonds, contracts, and contract payments to meet its mission as a regional water supplier for both current and future residents of communities in northeast Texas. NETMWD's enabling legislation subjects its bonds and contracts that secure those bonds, such as its wholesale water supply contracts with its member cities, to review and approval by the Attorney General.¹ Once approved by the Attorney General, the legality and

¹ See Sec.14, Chapter 78, Acts of the 53rd Legislature, Regular Session, 1953 (Article 8280-147, Vernon's Texas Civil Statutes).

validity of these contracts as public securities is established as a matter of law, and any future legal challenges regarding such validity is expressly prohibited under NETMWD's enabling legislation and multiple statutes.²

NETMWD and the reliability and enforceability of its wholesale water supply contracts, along with those of numerous other wholesale water suppliers across the state of Texas, will be negatively impacted if the ruling by the District Court is upheld. Wholesale water suppliers, their customers, and their investors depend on the reliability of long-term contracts negotiated at arm's length by sophisticated parties to allow the financing, construction, and operation of substantial and complex regional water supply systems. The legislature's adoption of a broad waiver of governmental immunity for such contracts³ ensures their enforceability and that governmental entities will be held responsible for their commitments. The Appellees and the District Court in this matter fail to recognize the important and unique role of regional water supply planners like SJRA and NETMWD in providing reliable and affordable wholesale water supplies. Upholding the findings by the District Court would effectively allow parties to long-term wholesale water supply contracts to re-negotiate those contracts at any time, making the bonds issued based

² See *id.*; see also TEX. GOV'T CODE §§ 1202.006(a) & 1371.059, TEX. WATER CODE § 49.184 (all providing independent statutory grounds for the incontestability of such contracts after approval by the Attorney General).

³ See TEX. LOCAL GOV'T CODE § 271.152.

on those contracts uncertain. That result would undermine the reliability of wholesale contracts in Texas, including those of NETMWD, drastically increase the cost to the public for water supply infrastructure, and likely serve as a bar to the implementation of many desperately needed water supply projects throughout the state.

NETMWD is responsible for payment of all legal fees and costs associated with the preparation of this amicus curiae brief.

SUMMARY OF THE ARGUMENT

If the District Court’s ruling is upheld, it will undermine the vast majority of long-term wholesale water supply contracts in the state and allow the parties under such contracts to effectively opt-out of their contractual obligations, leaving wholesale suppliers and purchasers without recourse to enforce their contracts. This result will create uncertainty and instability for both wholesale suppliers and purchasers and threaten the financial foundation on which long-term state and regional water supply planning in Texas depends. The Ninth Court of Appeals should reverse the District Court and find that the Groundwater Reduction Plan Contracts (“GRP Contracts”) between SJRA and the Appellees outlined the basic obligations and essential terms for performance, and therefore that Appellees waived their governmental immunity when entering into the GRP Contracts.

The Court has been presented with thorough legal analysis from SJRA regarding the Legislature’s broad waiver of governmental immunity under Local Government Code Section 271.152. The focus of this amicus brief is on the practical ramifications this case may have on water supply planning, financing, and development in Texas if the District Court’s ruling is upheld. NETMWD hopes to provide the Court with information related to how water suppliers in the state plan and finance long-term water supplies, and why the legislative waiver of governmental immunity for wholesale water supply contracts is imperative.

ARGUMENT

I. THE LEGISLATURE’S BROAD WAIVER OF GOVERNMENTAL IMMUNITY FOR WHOLESALE WATER SUPPLY CONTRACTS PROVIDES IMPORTANT PROTECTION AND STABILITY FOR THE FINANCING OF LONG-TERM WHOLESALE WATER SUPPLY PROJECTS ACROSS THE STATE OF TEXAS.

A. Texas utilizes long-term regional water supply planning efforts based on long-term water supply contracts, which are protected by holding governmental entities responsible for their commitments.

In making a determination regarding the applicability of the governmental immunity waiver in this matter, the Court should consider the impact its decision will have on Texas’ state water planning model, which relies on regional water supply development based in large part on long-term water supply contracts.

The Texas Water Development Board (“TWDB”) was created in 1957 in response to a significant drought experienced across Texas during the early 1950s.⁴ TWDB was, in part, charged with financing and helping to develop long-term water supply planning across the state. In 1997, in response to the drought of 1996, the Texas Legislature passed Senate Bill 1, overhauling how state water planning would be conducted in Texas.⁵ Senate Bill 1 created a stakeholder process in state water planning, directed drought contingency planning, emphasized conservation, and streamlined the state’s regulatory system. Through Senate Bill 1, the legislature

⁴ Tex. Const. art. III, § 49-c.

⁵ Senate Bill 1, Act of June 1, 1997, 75th Leg., R.S., ch. 1010, 1997 Tex. Gen. Laws 3610 (codified in TEX. WATER CODE ch. 16, subchapter C).

required that regional water planning groups be created to develop regional water plans, which are then submitted to the TWDB and adopted into a single state water plan. Often described as a “bottom-up” approach to state water planning, the current state water plan includes the work of sixteen regional water planning groups.⁶ The statutory framework for water planning is detailed, with a strong emphasis on public participation, open government processes, numerous opportunities for notice and comment, and the careful utilization of forecasting data for state growth and associated growth in water demand a half-century into the future. The Senate Bill 1 water planning process requires identification of water demands and needs, and of water supply projects to meet those demands and needs, on a 50-year rolling planning horizon to allow sufficient time for the research, planning, permitting, financing, and construction of large regional projects, which can take three or more decades in some instances to implement.

The ability of regional public water suppliers to implement the projects that are included in the regional and state water plans depends heavily on their ability to negotiate wholesale water contracts and pledge those contracts to secure the bonds issued to finance the water supply projects, which is the predominant financing mechanism for regional projects throughout the state. Such contracts provide the

⁶ See TEXAS WATER DEVELOPMENT BOARD, 2017 STATE WATER PLAN – Water for Texas (2017) available at <http://www.twdb.texas.gov/waterplanning/swp/2017/doc/SWP17-Water-for-Texas.pdf?d=504527>.

economic security necessary to allow suppliers to develop and maintain water supplies and the related infrastructure to meet various regional needs. Without assurance that governmental entities can be held responsible for their water supply contract commitments through tools like the legislative waiver of governmental immunity, those governmental entities may be able to essentially opt-out of their obligations during the term of the contract. If this is allowed, no regional water supplier will have the financial security afforded by such long-term contracts to continue to develop and maintain regional water supplies and no purchaser can be assured that water will continue to be supplied through the contracts it has executed to meet its current and future demands and needs.

B. If governmental entities are not held responsible for their commitments, the state's structure for long-term water supply planning will fail.

Regional water suppliers must finance the construction of facilities to provide the water supply needs outlined in the regional and state water plans. Such financing for capital assets like surface water reservoirs, water treatment plants, pipelines, and pump stations is often accomplished through the issuance of revenue bonds. To support the payment of debt service on the bonds issued by water suppliers such as SJRA and NETMWD, contracts are executed with cities and other political

subdivisions that will be purchasing the water supply on a wholesale basis.⁷ Because they are part of coordinated long-term regional water planning efforts, such contracts are often for a term of decades. In fact, the Texas Legislature recognized the distinct role of wholesale water supply contracts, unlike retail water contracts, in long-term water supply planning by allowing such wholesale contracts to be of unlimited duration or for the life of bonds for projects.⁸

The GRP Contracts at issue were the result of negotiations between SJRA and the Appellees under the representation of their own legal counsel. The Appellees benefitted from these contracts, allowing them to pursue growth knowing that they had dependable wholesale water supplies. SJRA bondholders rely on the terms of the contracts to make low-cost financing available for long-term water infrastructure projects. Just as SJRA cannot suddenly decide to no longer maintain or continue to develop certain water supplies needed to meet the water demands of the Appellees, the Appellees cannot decide to walk away from their financial obligations under the contracts. The legislature confirmed the enforceability of the GRP Contracts through an expansive waiver of governmental immunity.

II. THE USE OF A “RATE TIMES QUANTITY” FORMULA BASED ON A SEPARATE RATE ORDER ⁹ TO ESTABLISH PAYMENT OBLIGATIONS FOR WHOLESALE WATER SUPPLY CONTRACTS

⁷ See TEX. LOCAL GOV'T CODE § 552.012, TEX. WATER CODE § 49.213 (providing two of many statutory bases in Texas for contracting authority to support this method of finance).

⁸ See TEX. GOV'T CODE § 791.026(b)-(d).

⁹ GRP Contracts 6.02, CR.396-97.

IS WIDESPREAD, IS THE ACCEPTED WAY SUCH CONTRACTS ARE STRUCTURED IN TEXAS, AND PROVIDES THE NECESSARY “ESSENTIAL TERMS” FOR PURPOSES OF WAIVING GOVERNMENTAL IMMUNITY.

A. It is impracticable for long-term wholesale water supply contracts to specify a fixed price.

In suggesting that the scope of the Legislature’s governmental immunity waiver is limited to wholesale water supply contracts that specify a fixed price and volume of water,¹⁰ the Appellees fail to adequately recognize the long-term and unique nature of a wholesale water supply contract. As noted above, such contracts are for terms lasting many decades. It would be impracticable for such long-term contracts to set a fixed price when, over the course of the contract term, the cost of providing service under the contract will most certainly fluctuate.

NETMWD has wholesale water supply contracts with terms lasting 40 years and longer if outstanding debt is tied to the water supply. It is impossible to set an accurate price for the wholesale service of water 40 years in the future. The use of separate rate orders and fluctuating rates based on a formula or other objective standard clearly specified in the underlying contract allows suppliers to cover the ever-changing cost of service and inflation and to secure any additional water supplies needed in the future that may be unknown at the time the contract is executed, but necessary to satisfy the terms of the contract. Wholesale water service

¹⁰ Brief of Appellees, at p. 20.

is impacted by any number of factors, including the variable cost of purchasing electrical power, compliance with ever-changing state and federal treatment requirements, fluctuations in the price of water treatment chemicals and supplies, repair, replacement, and maintenance of water supply and treatment infrastructure and equipment, and other unpredictable operations and maintenance costs. The costs of these factors will certainly fluctuate over time, making a fixed price impossible to predict and utilize in the underlying contract.

The use of a formula-based pricing scheme with unknown variables in certain contracts is common and clearly authorized by law. Unlike SJRA's GRP Contracts, which state the essential price terms of the contracts by including a specific contractual formula to establish its water rates in conjunction with an "at lowest-cost" standard,¹¹ the Texas Business and Commerce Code authorizes parties to enter into binding contracts "though the price is not settled" and even if "nothing is said as to price."¹² In such contracts or contracts where the price is to be fixed by the seller, the price will be held to be "a reasonable price" and the seller must fix the price "in good faith."¹³ The Texas Supreme Court has upheld the validity of "open-term price" contracts in which gasoline refiners set a sale price to a posted price that

¹¹ Brief of Appellant, at pp. 26-27.

¹² See TEX. BUS. & COM. CODE § 2.305.

¹³ *Id.*

is fairly applied to similarly-situated purchasers.¹⁴ Likewise, courts have acknowledged that there is a presumption that parties intended a reasonable price when an agreement specifies a formula or other basis on which a reasonable price may be determined.¹⁵ In reviewing a wholesale water contract dispute, the Corpus Christi Court of Appeals upheld the validity of a contract much like the GRP Contracts, which contained an “open-term price” provision that calculated the sale price of wholesale water based upon a quantity and rate formula and the seller’s cost of service.¹⁶

The vast majority of wholesale water supply contracts in Texas do not include a fixed price in the contract. Suggesting that such contracts must contain a fixed price in order for the legislative governmental immunity waiver to apply to those contracts will upend all similar contracts between governmental entities and cause chaos in Texas’ water financing system. Ultimately, such a system will increase the cost of water for the public as water suppliers will be forced to raise prices to cover the cost of uncertainty.

B. Wholesale water supply contracts like the GRP Contracts provide the “essential terms” necessary to waive governmental immunity.

¹⁴ *Shell Oil Co. v. HRN, Inc.*, 144 S.W.3d 429, 436 (Tex. 2004).

¹⁵ *See David J. Sacks, P.C. v. Haden*, 266 S.W.3d 447, 450 (Tex. 2008) (holding that, although the parties did not specify an exact total price, their agreement to use hourly rates confirmed that they intended a reasonable price).

¹⁶ *Canyon Regional Water Authority v. Guadalupe-Blanco River Authority*, 286 S.W.3d 397, 403-404 (Tex. App.—Corpus Christi 2008).

In order for governmental immunity to be waived under a wholesale water supply contract, the contract must provide “the essential terms of the agreement.”¹⁷ As briefed and addressed by SJRA, this requirement has been interpreted by the Texas Supreme Court to mean that the “basic obligations” of the contract must be clearly outlined.¹⁸ Wholesale water supply contracts that provide a formula-based price calculation, like the GRP Contracts and NETMWD’s wholesale contracts, provide sufficient detail for purposes of price and volume to clear this bar. As addressed above, the price of water under most wholesale water supply contracts is based on a formula that is tied to a rate order or rate schedule. When entering into the contract, the purchaser knows that the price they will pay is based on a specific formula: the volume of water to be taken¹⁹ multiplied by the rate order or schedule constructed to address unknown costs in supplying water.

For this Court to find that a constant, non-variable price amount must be set in a wholesale water supply contract in order for that contract to address the “basic obligations” of the parties would be to find that virtually no long-term wholesale water supply contract with a governmental entity can ever be enforced due to governmental immunity. Such an outcome would cause uncertainty across the state

¹⁷ TEX. LOCAL GOV’T CODE § 271.151(2)(A).

¹⁸ *Kirby Lake Dev., Ltd. v. Clear Lake City Water Auth.*, 320 S.W.3d 829, 838 (Tex. 2010).

¹⁹ Like the GRP Contracts, NETMWD has wholesale water supply contracts that set a certain take-or-pay minimum that is used for calculating the price to be paid. NETMWD also has some wholesale contracts that do not require any minimum water purchase.

in water supply planning and financing, allowing governmental entity-purchasers to simply change their mind based on political whims if they do not want to pay under a wholesale water supply contract and allowing governmental entity-providers to stop service if they find a better customer that comes along for a higher price. For the stability and security of water supply planning and the water supply financing bond markets, in which the State of Texas through its agency the Texas Water Development Board and the citizens of Texas have a substantial investment and stake, and as clearly authorized and required by the statutes and common law of this state, governmental entities must be held accountable through the statutory waiver of governmental immunity for the fluctuating-price contracts they enter into and upon which wholesale providers finance water projects.

C. Long-term water supply development in Texas favors reversing the lower court's decision regarding the applicability of the governmental immunity waiver.

The impact of the Court's ruling in this matter will have wide-spread implications for water supply providers in Texas. Appellees criticize SJRA for raising the fact that the District Court's ruling jeopardizes the enforceability of other municipal water supply contracts that utilize a formula-based rate structure.²⁰ However, if the Court upholds the applicability of governmental immunity in this

²⁰ Brief of Appellees, at pp.31-34.

matter as the Appellees propose, there will be an unavoidable negative impact on the financing of long-term wholesale water supplies in Texas due to the uncertainty of rate and contract stability. Without the protection afforded by the Legislature's waiver of governmental immunity, financial lenders will recognize that purchasers under a wholesale contract have the ability to re-negotiate their rate essentially at any time (because suppliers do not have the ability to enforce their contracts), making an investment in water supply projects inherently riskier. Potential purchasers, when negotiating with a wholesale supplier, will be less careful regarding the terms to which they commit knowing that they can back out of such obligations. The ultimate cost of long-term water supply projects will increase under these circumstances as borrowing costs in the bond markets will predictably respond to the increased risk and unreliability of long-term wholesale contracts. Such costs will ultimately be passed along to the citizens of Texas in the form of substantially increased water rates.

PRAYER

For the reasons expressed in this brief, the Ninth Court of Appeals should reverse the decision of the Montgomery County District Court granting the Appellees' plea to the jurisdiction and remand the matter for trial.

Respectfully submitted,

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Ramon G. Viada	20559350	rayviada@viadastrayer.com	11/13/2020 1:20:54 PM	SENT
Michael V. Powell	16204400	mpowell@lockelord.com	11/13/2020 1:20:54 PM	SENT

Associated Case Party: City of Magnolia, Texas

Automated Certificate of eService

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Lindsey Smith on behalf of Michelle Smith
Bar No. 24043929
lsmith@sledgelaw.com
Envelope ID: 48081265
Status as of 11/13/2020 1:35 PM CST

Associated Case Party: City of Magnolia, Texas

Name	BarNumber	Email	TimestampSubmitted	Status
Leonard V. Schneider	17792500	lschneider@liles Parker.com	11/13/2020 1:20:54 PM	SENT
Michael V. Powell	16204400	mpowell@lockelord.com	11/13/2020 1:20:54 PM	SENT

Associated Case Party: Utilities Investment Co., Inc.

Name	BarNumber	Email	TimestampSubmitted	Status
Marvin Jones	10929100	marty.jones@sprouselaw.com	11/13/2020 1:20:54 PM	SENT
Cullom Jones	24079808	brantley.jones@sprouselaw.com	11/13/2020 1:20:54 PM	SENT

Associated Case Party: T&W Water Service Company

Name	BarNumber	Email	TimestampSubmitted	Status
Marvin Jones	10929100	marty.jones@sprouselaw.com	11/13/2020 1:20:54 PM	SENT
Cullom Jones	24079808	brantley.jones@sprouselaw.com	11/13/2020 1:20:54 PM	SENT