



## Spotlight On

# PUBLIC FINANCE

## Summer 2016 Newsletter

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## FEATURED ARTICLE

### TEXAS SUPREME COURT DECISIONS REVEAL CRACKS IN GOVERNMENTAL IMMUNITY

By Jonathan Frels and Sandra Staine

Though less than six-months old, 2016 is already a momentous year in Texas governmental immunity jurisprudence. In April, the Texas Supreme Court released three significant governmental immunity decisions that suggest the court is pivoting toward the protection of private interests in dealings with municipalities in some circumstances. In *Wasson Interests v. City of Jacksonville*<sup>1</sup> and *Wheelabrator Air Pollution Control v. City of San Antonio*,<sup>2</sup> the court squarely addressed the applicability of the proprietary-governmental dichotomy in breach of contract claims for the first time, concluding that a municipality does not have governmental immunity when it performs proprietary functions.<sup>3</sup> In *Houston Belt & Terminal Railway et al v. City of Houston*,<sup>4</sup> the court clarified the breadth of sovereign immunity for ultra vires actions of government officials, holding that while governmental immunity bars suits complaining of an exercise of *absolute* discretion, it “does not bar suits complaining of either an officer’s failure to perform a ministerial act or an officer’s exercise of judgment or limited discretion without reference to or in conflict with the constraints of the law authorizing the official to act.”<sup>5</sup>

#### Applying the Proprietary-Governmental Dichotomy in the Breach of Contract Context

Sovereign immunity is inherent in statehood and generally protects the state from suits for money damages.<sup>6</sup> Political subdivisions of the state share in the state’s inherent immunity, which is referred to as governmental immunity when applied to political subdivisions.<sup>7</sup> The practical purpose of governmental immunity is to shield the public from the costs and consequences of the improvident actions of their government, and a political subdivision’s immunity extends only as far as the state’s immunity.<sup>8</sup> As a result, the courts have distinguished between those acts performed by a municipality as a branch of the state and those undertaken in the performance of its proprietary, or non-governmental, functions.<sup>9</sup> In the tort claims context, the courts have long held that a municipality is not immune from torts committed in its proprietary capacity.<sup>10</sup>

Prior to its decisions in *Wasson and Wheelabrator*, the Court had only briefly analyzed the applicability of the proprietary-governmental dichotomy in the breach of contract context. In *Tooke vs. City of Mexia*,<sup>11</sup> the Court concluded that the actions of the city at issue were undertaken in the performance of the city's governmental functions and refused to determine whether the dichotomy should be extended to breach of contract claims.<sup>12</sup> The *Tooke* decision did, however, establish that when governmental immunity does apply it is only waived by clear and unambiguous language.<sup>13</sup> Following *Tooke*, several courts concluded that a municipality was never subject to suit in a breach of contract claim absent a legislative waiver of immunity.<sup>14</sup>

In *Wasson*, the Court rejected that view, explaining that “the state generally enjoys immunity for its lawful functions, which are undertaken on behalf of the ‘the people[,]’”<sup>15</sup> and political subdivisions of the state share in the state's immunity “when acting as the state's agent and performing governmental functions for the public's benefit.”<sup>16</sup> However, municipal acts that are proprietary in nature are not done as a branch of the state, but rather “for the advantage and benefit of the locality and its inhabitants.”<sup>17</sup> As a result, such actions do not implicate the state's immunity because “they are not performed under the authority or for the benefit of the sovereign.”<sup>18</sup> In other words, it is not necessary to look for a legislative waiver of immunity in breach of contract actions when a municipality is acting in its proprietary capacity because those actions are not protected by governmental immunity.

The court acknowledged that the distinction between governmental and proprietary acts is not always clear.<sup>19</sup> However, the Court noted that Article XI, section 13(a) of the Texas Constitution authorizes the legislature to “define for all purposes those functions of a municipality that are to be considered governmental and those that are proprietary, including reclassifying a function's classification assigned under prior statute or common law.”<sup>20</sup> In the tort-claims context, the legislature has undertaken to define specific functions as governmental or proprietary through the Tort Claims Act.<sup>21</sup>

Having decided in *Wasson* that municipalities do not have immunity from suit for breach of contract claims where the municipality is performing a proprietary function, the *Wheelabrator* case presented the Court with the question of whether (i) a contract to install pollution control equipment at a power plant was proprietary or governmental in nature and (ii) a claim for attorney's fees arising from a breach of that contract implicated governmental immunity.<sup>22</sup> The Court endorsed the use of the Tort Claims Act as a guide in classifying municipal actions as proprietary or governmental in nature – and thus the boundaries of immunity – in a breach of contract action.<sup>23</sup> Relying on guidance from the Tort Claims Act and the common law, the Court determined that the operation of a public utility, in this case a municipally-owned electric and gas utility, was a proprietary function.<sup>24</sup> As a result, the public utility was not shielded by governmental immunity, and the claim for attorney's fees arising from a contract undertaken in a proprietary capacity was not barred by governmental immunity.

Taken together, *Wasson* and *Wheelebrator* significantly change the landscape for entities contracting with municipalities when the municipality is acting in a proprietary capacity. Where an action arises out of a municipality's performance of a proprietary function, a municipality is subject to suit in the same manner as any private person. Municipalities and the entities with whom they contract are then left with the question of when a municipality is acting in its proprietary capacity. The Tort Claims Act defines the proprietary functions of a municipality as those functions that a municipality may, in its discretion, perform in the interest of the inhabitants of the municipality, including but not limited to:

- (1) the operation and maintenance of a public utility;
- (2) amusements owned and operated by the municipality; and
- (3) any activity that is abnormally dangerous or ultrahazardous.<sup>25</sup>

The Tort Claims Act makes clear that the proprietary functions of a municipality do *not* include the 36 categories of governmental activities listed under Section 101.0215(a).<sup>26</sup> Those 36 categories include a significant portion of the activities undertaken by municipalities, including the operation of water and sewer systems, transportation systems, parks and recreational facilities and parking facilities.<sup>27</sup> As a result, it appears that the most immediate impact of recent decisions will be felt in contracts with municipally-owned electric and gas utilities.

## The Ultra Vires Exception to Governmental Immunity

Texas law recognizes that governmental immunity protects certain exercises of discretion by governmental officials. However, Texas courts “have long recognized that governmental immunity does not bar claims alleging that a governmental officer acted *ultra vires*, or without legal authority, in carrying out his duties.”<sup>28</sup>

*Houston Belt & Terminal Railway et al. v. City of Houston* clarified the breadth of governmental immunity for *ultra vires* actions of government officials. The case involved the administration of a city's drainage-fee ordinance. The ordinance gave the city's

Director of Public Works and Engineering (the “Director”) the authority to administer the provisions of the ordinance, subject to the provisions of the ordinance. Under the ordinance, drainage fees were to be assessed based on whether or not a property was “benefitted” or contained “impervious surface,” and provided guidance in how to assess whether property was benefitted or impervious. At issue was whether the Director, in allegedly improperly following the guidance of the ordinance when assessing the drainage fee, was subject to *ultra vires* claims. The city argued that the Director’s determinations could not be *ultra vires* if he had some discretion to make them under the ordinance.

The Court clarified while governmental immunity bars suits complaining of an exercise of *absolute* discretion, it “does not bar suits complaining of *either* an officer’s failure to perform a ministerial act *or* an officer’s exercise of judgment *or limited* discretion without reference to or in conflict with the constraints of the law authorizing the official to act.”<sup>29</sup> In other words, governmental immunity extends only to those government officers acting in a manner that is consistent with the law. The Court explained that “prohibiting *ultra vires* suits when an officer acts outside of his the bounds of his granted authority would run counter to the purpose of immunity.”<sup>30</sup>

While seemingly expanding the *ultra vires* exception, the Court cautioned against treating the decision as “a new vehicle for suits against the state to masquerade as *ultra vires* claims.”<sup>31</sup> The court noted that while only the exercise of absolute discretion is absolutely protected, the breadth of the grant of authority in issue in a particular case will govern whether a suit attacking the exercise of discretion would be barred by governmental immunity. The more discretion given to a governmental official by the law, the more likely it is that the officials’ actions would be protected.

## Conclusion

There are several important takeaways from the Court’s holdings in *Wasson*, *Wheelabrator* and *Houston Belt & Terminal Railway*. The first is the clear understanding that acts performed in the exercise of a municipality’s proprietary functions are not afforded the protection of governmental immunity. For private entities contracting with municipalities in contexts such as electric or gas utilities, these decisions remove some significant complications related to their ability to enforce contractual arrangements. The second is the recognition of the legislature’s ability to classify – and reclassify – municipal functions as governmental or proprietary. While long recognized in the tort-claims context, the application of the proprietarygovernmental dichotomy in the breach of contract context is likely to open new legislative battles and create legal questions regarding the impact of future legislative changes on existing contracts. Finally, the expansion of the *ultra vires* exception would appear to give private entities greater opportunities to challenge the administrative implementation or application of laws.

*For questions about the governmental immunity cases described in this article and the effect that they might have on you, please do not hesitate to contact the authors or any of Bracewell’s public finance team.*

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<sup>1</sup> No. 14-0645, 2016 WL 1267697 (Tex. Apr. 1, 2016).

<sup>2</sup> No. 15-0029 (Tex. Apr. 15, 2016), available at <http://docs.texasappellate.com/scotx/op/15-0029/2016-04-15.green.pdf>.

<sup>3</sup> *Wasson* at \*9.

<sup>4</sup> No. 14-0459, 2016 WL 132910 (Tex. Apr. 1, 2016).

<sup>5</sup> *Id.* at \*5 (emphasis in original).

<sup>6</sup> *Wasson* at \*1.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> *Id.*

<sup>11</sup> 197 S.W.3d 325 (Tex. 2006).

<sup>12</sup> See *Tooke*, *supra* note 6 at 343 (“But we have never held that this same distinction determines whether immunity from suit is waived for breach of contract claims, and we need not determine that issue here.”).

<sup>13</sup> *Id.* at 332-33.

<sup>14</sup> See, e.g., *City of San Antonio v. Wheelabrator Air Pollution Control, Inc.*, 381 S.W.3d 597 (Tex. App.—San Antonio 2012, pet. denied).

<sup>15</sup> *Wasson* at \*4.

<sup>16</sup> *Wasson* at \*4 (citing *City of Galveston v. State*, 217 S.W.3d 466, 478 (Tex. 2007) (Willett, J., dissenting)).

<sup>17</sup> *Id.* at \*4 (citing *City of Galveston v. Posnainsky*, 62 Tex. 118, 127 (Tex. 1884)).

<sup>18</sup> *Id.* at \*4.

<sup>19</sup> *Id.* at \*9.

<sup>20</sup> Tex. Cons. art. XI, §13(a).

<sup>21</sup> Tex. Civ. Prac. & Rem. Code §101.0215 (West 2016).

<sup>22</sup> *Wheelabrator* at \*1.

<sup>23</sup> *Id.* at \*6.

<sup>24</sup> *Id.*; see also Tex. Civ. Prac. & Rem. Code §101.0215(b)(1) (West 2016).

<sup>25</sup> Tex. Civ. Prac. & Rem. Code §101.0215(b)(1) (West 2016).

<sup>26</sup> *Id.* at §101.0215(a). Section 101.0215(a) defines the governmental functions of a municipality as follows:

(a) A municipality is liable under this chapter for damages arising from its governmental functions, which are those functions that are enjoined on a municipality by law and are given it by the state as part of the state's sovereignty, to be exercised by the municipality in the interest of the general public, including but not limited to:

- (1) police and fire protection and control;
- (2) health and sanitation services;
- (3) street construction and design;
- (4) bridge construction and maintenance and street maintenance;
- (5) cemeteries and cemetery care;
- (6) garbage and solid waste removal, collection, and disposal;
- (7) establishment and maintenance of jails;
- (8) hospitals;
- (9) sanitary and storm sewers;
- (10) airports, including when used for space flight activities as defined by Section 100A.001;
- (11) waterworks;
- (12) repair garages;
- (13) parks and zoos;
- (14) museums;
- (15) libraries and library maintenance;
- (16) civic, convention centers, or coliseums;
- (17) community, neighborhood, or senior citizen centers;
- (18) operation of emergency ambulance service;
- (19) dams and reservoirs;
- (20) warning signals;
- (21) regulation of traffic;
- (22) transportation systems;
- (23) recreational facilities, including but not limited to swimming pools, beaches, and marinas;
- (24) vehicle and motor driven equipment maintenance;
- (25) parking facilities;
- (26) tax collection;
- (27) firework displays;
- (28) building codes and inspection;
- (29) zoning, planning, and plat approval;
- (30) engineering functions;
- (31) maintenance of traffic signals, signs, and hazards;
- (32) water and sewer service;
- (33) animal control;
- (34) community development or urban renewal activities undertaken by municipalities and authorized under Chapters 373 and 374, Local Government Code;
- (35) latchkey programs conducted exclusively on a school campus under an interlocal agreement with the school district in which the school campus is located; and
- (36) enforcement of land use restrictions under Subchapter E, Chapter 212, Local Government Code.

<sup>27</sup> *Id.* at §101.0215(c).

<sup>28</sup> *Houston Belt & Terminal Railway* at \*1.

<sup>29</sup> *Id.* at \*5 (emphasis in original).

<sup>30</sup> *Id.* at \*6.

<sup>31</sup> *Id.*

# BRACEWELL UPDATES

Originally published in February of this year, the Internal Revenue Service's proposed Treasury Regulations that would impose new requirements on entities seeking to qualify as a "political subdivision" (the "Proposed Regulations") are back in the news as written comments on the Proposed Regulations were due on May 23. Over a hundred sets of comments in opposition to the Proposed Regulations were submitted to the Treasury Department ("Treasury"), and many organizations called for their withdrawal. Bracewell, together with the law firms of Allen Boone Humphries Robinson LLP and Schwartz, Page & Harding L.L.P., submitted comments on behalf of an interest group relating to Texas special districts. The comments called first for withdrawal, but also proposed alternatives for consideration by the IRS and Treasury. For a short overview of the Proposed Regulations, please visit <http://www.bracewelllaw.com/news-publications/updates/proposed-regulations-could-have-substantial-effect-special-district-issuer>.

## PRACTICE FOCUS

### TRANSPORTATION

Bracewell is truly a one-stop-shop for structuring finance options for our transportation clients. Our attorneys advise clients in connection with a variety of legal issues that emerge during the course of funding of transportation and mobility projects. From infrastructure development and construction to public contracting and financing, we combine our diverse experience to assist our clients with a broad base of issues. This broad cross-over assures our clients that they will have access to attorneys who are well-versed in regulatory, antitrust, litigation, transactional, technology, and governmental affairs matters cutting across all modes of transportation.

Bracewell public finance attorneys have been key participants in many of the major transportation and mobility public finance developments in the southwest region of the nation. Our attorneys are experienced in representing clients in the financing of transportation projects, including the issuance of toll revenue bonds, vehicle registration fee bonds, bridge revenue bonds, general obligation bonds, certificate of obligations, and contract revenue obligations (including pass-through revenue obligations).

Bracewell has a wealth of experience as bond and underwriter's counsel, having been involved with a number of Texas complex transportation financings involving multiple sources of funding. With respect to federal law and regulation relating to disclosure requirements, Bracewell partner Paul Maco provides a unique combination of extensive experience in establishing SEC disclosure policy, defending issuers, issuer officials, bond counsel and underwriters in SEC investigations, serving as disclosure, bond and underwriters' counsel in municipal securities offerings, and preparing and implementing disclosure policies and procedures and training issuer officials and employees in their use.

Attorneys at Bracewell have advised public and private clients on local, state and federal procurement and contractor guidelines for transportation projects. We are familiar with funding guidelines and grant applications and compliance. Additionally, our attorneys have advised our clients on virtually every type and variation of transportation development contract and infrastructure tool available, including, but not limited to, concessions; design-build; TIFIA loans and other federal grants and loans; transit related development; lease-lease back and lease purchase agreements; transportation and tax increment reinvestment zones.

Our attorneys were on the forefront in drafting much of the Texas legislation creating public transit authorities, and we continue our representations today. Bracewell provides government relations services at both the federal and state levels and understands the regulatory and financial requirements specific to transportation authorities. Furthermore, the firm's Policy Resolution Group serves our clients in matters in Congress and the regulatory agencies.

While infrastructure demands in Texas continue to expand, transportation clients can rely on Bracewell's team of attorneys to help navigate any complex legal issues that such entities may face. If you are interested in learning more about our transportation practice, please contact Glenn Opel, Barron Wallace, Blakely Fernandez, Elizabeth Bowes or Tim Deithloff.

# ATTORNEYS IN ACTION

## International Citizen of the Year

Jane Macon is the recipient of The World Affairs Council of San Antonio's 2016 International Citizen of the Year award. Macon, a "pioneer in women's leadership," was recognized for her "contributions to the international community [which] truly exemplify global citizenship." She was honored at the 2016 International Citizen of the Year Gala, held Thursday, February 25. Bracewell Senior Counsel Kay Bailey Hutchison served as host of the event.

## Dallas Bar Foundation (DBF) Fellows

Glenwood F. Hill II was elected to membership in the Fellows of the DBF. DBF Fellows are Dallas attorneys who have distinguished themselves in their legal careers and in their civic contributions and are nominated by current DBF Fellows.

## Texas City Attorneys Association (TCAA)

*June 15 - 17, 2016, Bastrop, TX*

Derrick Mitchell and Glenwood Hill will deliver a speech titled "How to Deal with Bond Counsel" at the TCAA Summer Conference at the Hyatt Lost Pines Resort and Spa in Bastrop.

## National Society of Compliance Professionals

*October 18, 2016, Washington, DC*

Paul Maco is participating on a panel titled "Overview of 2016 SEC/FINRA/MSRB Notices and Guidance" for the National Society of Compliance Professionals National Conference.

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## EVENTS

### SPOTLIGHT ON PUBLIC FINANCE LUNCH AND LEARN: GOVERNMENTAL IMMUNITY

#### Wednesday, June 22

11:30 am- 1:00 pm

Lunch will be provided.

#### Bracewell LLP

111 Congress Avenue, Suite 2300

Austin, TX 78701

+1.512.472.7800

Though less than six-months old, 2016 is already a momentous year in Texas governmental immunity jurisprudence. The Texas Supreme Court recently released three significant governmental immunity decisions. In *Wasson Interests v. City of Jacksonville* and *Wheelabrator Air Pollution Control v. City of San Antonio*, the Court established that when a municipality is performing proprietary functions it does not enjoy governmental immunity from suit in a breach of contract context. Then the Court clarified the breadth of governmental immunity for ultra vires actions of government officials in *Houston Belt & Terminal Railway et al v. City of Houston*. What does this mean for your organization and how should you respond? Bracewell Partners Elizabeth Bowes and Glenn Opel will answer the following:

- What is a proprietary vs. governmental function?
- What does a municipality not having governmental immunity mean for your organization?
- What are ultra vires actions?

To register, contact Alisa Tristan at [alisa.tristan@bracewelllaw.com](mailto:alisa.tristan@bracewelllaw.com) or 713.223.1279.

*1.0 hour of CPE credit pending.*

*1.0 hour of MCLE participatory credit pending.*

# ATTORNEY SPOTLIGHT



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Glenn serves as bond counsel, underwriter's counsel, and letter of credit bank counsel in public finance transactions involving cities, counties, school districts, universities, regional mobility authorities, municipal utility districts, river and port authorities, and state agencies.

## **What are your specialties within public finance?**

My practice focus is on infrastructure and transportation development and local government issuers, specifically cities, counties, and schools. Throughout the course of the last 25 years, I've also worked on a wide range of financing transactions for a variety of issuers, including public/private partnerships, industrial development, special districts, and state agencies.

## **What do you like best about public finance practice?**

When issuers go through the bond process, it's never simple or one-sized-fits-all. I get the opportunity to work with clients who are seeking help and walk them through the myriad of issues. Clients appreciate my help and that's what it's all about. By the time the bond has closed, we've been through the trenches and made it through to the other side together.

## **How do you like to spend your time outside of work?**

Any chance I get, I'm outdoors. You can find me on the Town Lake hike and bike trails five or six days a week running with my wife. And now that our Austin area lakes have water, I like to spend my weekends on the water.

## **What is your favorite thing about Austin?**

What sets Austin apart is its laid-back mentality and love of outdoor activities – the trails, parks, concerts, rivers, lakes, and patio bars and restaurants. It is a great place to work hard and raise a family but still not take yourself too seriously. I think it's great that we still have Eeyores Birthday Party here every year!

## **Would you rather be able to visit 100 years in the past or 100 years in the future?**

Assuming I could meet anyone I wanted, I'd visit 100 years ago. I would like to meet my great-grandparents and my grandparents when they were young, and a few other folks like Winston Churchill, George Patton, Albert Einstein, Bertrand Russell, Claude Monet, and my favorite author J.R.R. Tolkien.

# BRACEWELL BY THE NUMBERS

**44**

Number of transit and tollway transactions for which Bracewell was bond counsel since 2013

**\$6.2 billion**

Total par amount of transit and tollway transactions with Bracewell attorneys as bond counsel and special tax counsel since 2013

**15**

Number of Bracewell transportation and mobility public finance clients

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## DID YOU KNOW?

- The principle of sovereign immunity is commonly expressed by the popular legal maxim “rex non potest peccare,” or “the king can do no wrong.”
  - The longest segment of Interstate Highway in Texas is I-10 at 878.6 miles (1,414.0 km); the shortest is I-110 at 0.9 miles (1.4 km).
  - Toll roads have a long history. As far back as 7th century BC, tolls had to be paid by travelers using the Susa-Babylon highway.
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*Bracewell LLP is a leading law and government relations firm serving the oil and gas, power, financial services, technology and public finance industries throughout the world. Our industry focus enables us to maintain cutting-edge experience and in-depth knowledge of the commercial, legal and regulatory challenges faced by our clients so that we can provide the most effective legal solutions to facilitate transactions and resolve disputes.*