Presented:
Dallas Bar Association

March 11, 2019
Dallas, Texas

EXPLORING SOVEREIGN IMMUNITY ISSUES IN REAL ESTATE TRANSACTIONS

Arthur J. Anderson

Author contact information:
Arthur J. Anderson
Winstead PC
Dallas, Texas

aanderson@winstead.com
214-745-5745

I. Introduction

Sovereign immunity is an outdated, unfair concept that should be abolished. The doctrine was originally justified by the fiction that "the king can do no wrong," *id.* (citing 3 William Blackstone, Commentaries on the Laws of England 254 (1768)). But there are few legal theories created in the Middle Ages that exist today. In fairness, governmental entities should be obligated to obey statutory and common law principles like the rest of us. The often cited reasons for the concept are no longer valid:

a. Precedent. In *Harris County Hospital District v. Tomball Regional Hospital*, 283 S.W.3d 838 (Tex. 2009), the Texas Supreme Court noted that the sovereign immunity doctrine had been established in Texas since the mid-nineteenth century which apparently was reason enough to sustain it. This begs the question as to why precedent prevails over the need to compensate for wrongful acts by governmental entities.

b. Financial Resources. In *Tooke v. City of Mexia*, the Texas Supreme Court observed that immunity "shield[s] the public from the costs and consequences of improvident actions of their governments." 197 S.W.3d 325, 332 (Tex. 2006). This position overlooks one of the intended purposes of tax resources which is to protect the public against harmful actions of the government itself.

Large municipalities have significant resources to defend themselves against lawsuits. The City of Dallas has a $3 billion annual budget and dozens of assistant city attorneys who litigate cases. Even my old home town Lubbock, Texas has a budget in excess of $100,000,000.00. Comparing the financial resources of potential litigants weighs heavily in favor of abolishing the immunity defense.

c. Meritless Suits. Some cities argue that without the immunity shield they will be forced to defend meritless lawsuits. But the Rules of Civil Procedure provide sufficient protection. According to TRCP 13, sanctions can be imposed if a frivolous lawsuit is filed against a city.

Instead of clearing the deck and allowing private litigants to sue governmental entities in legitimate lawsuits, the courts and the Legislature instead draw fine distinctions as to when immunity does or does not apply. For example, why is immunity waived when the validity of an ordinance is challenged but not when the text of the ordinance needs a judicial interpretation? Why are some functions listed in the Texas Torts Claims Act considered to be governmental while others are not? Abolishing the concept of immunity would level the playing field for everyone.

II. Sovereign Immunity Principles

Although courts frequently conflate the terms and the concepts, the State of Texas and its political subdivisions are imbued with distinct forms of immunity: sovereign or governmental. Unlike the State, which through *sovereign* immunity enjoys the greatest level of protection from suit and liability, municipalities are relegated to *governmental* immunity. *Wichita Falls State Hosp. v. Taylor*, 106 S.W.3d 692, 694 (Tex. 2003) ("Governmental immunity, on the other hand,

protects political subdivisions of the State, including counties, cities, and school districts.") (citing *City of LaPorte v. Barfield*, 898 S.W.2d 288, 291 (Tex. 1995)).

Sovereign immunity has two components: immunity from suit and immunity from liability. *Gen. Servs. Comm'n v. Little-Tex Insulation Co.*, 39 S.W.3d 591, 594 (Tex. 2001). First, the state retains immunity from suit unless it has been expressly waived by the Legislature. *Fed. Sign v. Tex. S. Univ.*, 951 S.W.2d 401, 405 (Tex. 1997). The Legislature has mandated that a statute shall not be construed as waiving immunity absent "clear and unambiguous language." TEX. GOV'T CODE § 311.034. The Texas Supreme Court has similarly held that, to effectively waive sovereign immunity, "a statute or resolution must contain a clear and unambiguous expression" of the State's waiver. *Wichita Falls State Hosp. v. Taylor*, 106 S.W.3d 692, 696 (Tex. 2003). A plaintiff must affirmatively demonstrate the court's subject-matter jurisdiction "by alleging a valid waiver of immunity." *See Dallas Area Rapid Transit v. Whitley*, 104 S.W.3d 540, 542 (Tex. 2003).

III. Pleas to the Jurisdiction

A municipality will usually file a plea to the jurisdiction in an attempt to dismiss or delay the plaintiff's land use lawsuit. The plea is the appropriate mechanism to address the immunity defense. By filing a plea to the jurisdiction, the government challenges the trial court's power to exercise subject-matter jurisdiction over the case. A plea to the jurisdiction is a dilatory plea which is used to defeat a plaintiff's cause of action without regard to whether the plaintiff's claims have merit. *See Bland Indep. Sch. Dist. v. Blue*, 34 S.W.3d 547, 554 (Tex. 2000). The question of whether a trial court properly exercised subject matter jurisdiction over a case is reviewed as a question of law. *Tex. Dep't of Parks & Wildlife v. Miranda*, 133 S.W.3d 217, 226 (Tex. 2004). Courts apply a *de novo* standard when reviewing trial court rulings on pleas to the jurisdiction. *Tex. Nat. Res. Conservation Comm'n v. IT-Davy*, 74 S.W.3d 849, 855 (Tex. 2002). If the city prevails on the immunity defense, then there is no trial or ruling on the merits of the plaintiff's case because the petition is dismissed.

IV. Proprietary v. Governmental

The first step in determining whether or not immunity applies to a land use dispute is to determine if a governmental or proprietary function is involved. The State enjoys sovereign immunity because "the State can only act in its governmental capacity," and the "distinction between proprietary and governmental functions does not apply to functions performed by the State". *Hencerling v. Texas A&M Univ.*, 986 S.W.2d 373, 374-75 (Tex. App.—Houston [1st District] 1999, pet. denied) (citing *Guillory v. Port of Houston Auth.*, 845 S.W.2d 812, 814-15 (Tex. 1993)). Municipalities, however, are subject to the proprietary/governmental dichotomy (the "Dichotomy"). Id. at 375.

A. Analysis of the Dichotomy

Whether governmental immunity exists depends on the resolution of the Dichotomy, i.e., whether the city was engaged in a governmental or proprietary function or activity. *City of Galveston v. Posnainky*, 62 Tex. 118, 127 (1884); *Gates v. City of Dallas*, 704 S.W.2d 737, 739

(Tex. 1986); *see also Ben Bolt-Palito Blanco Consol. Indep. Sch. Dist. v. Tex. Political Subdivisions Property/Casualty Joint Self-Ins. Fund*, 212 S.W.3d 320, 327 (Tex. 2006).

According to the Texas Supreme Court, "[m]unicipal corporations exercise their broad powers through two different roles: proprietary and governmental." *Gates*, 704 S.W.2d at 738. Governmental functions are generally defined as "those acts which are public in nature and performed by the municipality as the agent of the State in furtherance of general law for the interest of the public at large." *Id*. at 738 (internal cites omitted); *see also* Tex. Civ. Prac. & Rem. Code § 101.0215(a) (2015) (defining governmental functions as "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"). Proprietary functions, however, "are those functions performed by a city, in its discretion, primarily for the benefit of those within the corporate limits of the municipality." *Gates*, 704 S.W.2d at 739; see also Tex. Civ. Prac. & Rem. Code § 101.0215(b) (describing proprietary functions as "those functions that a municipality may, in its discretion, perform in the interest of the inhabitants of the municipality"). "Unlike governmental functions, for which municipal corporations have traditionally been afforded some degree of governmental immunity, proprietary functions have subjected municipal corporations to the same duties and liabilities as those incurred by private persons and corporations." *Gates*, 704 S.W.2d at 739; *Ethio Express Shuttle Serv. v. City of Houston*, 164 S.W.3d 751, 754 (Tex. App.—Houston [14th Dist.] 2005, no pet.).

In regard to governmental immunity, the Texas Supreme Court in *Wasson* "has distinguished between those acts performed as a branch of the state and those acts performed in a proprietary, nongovernmental capacity." *Wasson Interests, Ltd. v. City of Jacksonville*, 489 S.W.3d 427, 430 (Tex. 2016). A municipality is immune for acts done as a branch of the state referred to as governmental functions. *Id.* at 433. Governmental functions are "functions that are enjoined on a municipality by law ... to be exercised by the municipality in the interest of the general public." *See* Tex. Civ. Prac. & Rem. Code Ann. § 101.0215(a) (West Supp. 2017).

"[S]overeign immunity does not[, however,] imbue a city with derivative immunity when it performs proprietary functions." *Wasson Interests, Ltd.*, 489 S.W.3d at 43 Proprietary functions are "functions that a municipality may, in its discretion, perform in the interest of the inhabitants of the municipality." *See* Tex. Civ. Prac. & Rem. Code Ann. § 101.0215(b).

A city is not immune in performing a proprietary function regardless of "whether a city commits a tort or breaches a contract, so long as in each situation the city acts of its own volition for its own benefit and not as a branch of the state." *Wasson Interests, Ltd.*, 489 S.W.3d at 439. Therefore, "the common-law distinction between governmental and proprietary acts-known as the proprietary-governmental dichotomy-applies in the contract-claims context just as it does in the tort-claims context." *Id.; see also Jamro Ltd. v. City of San Antonio,* No. 04-16-00307-CV, 2017 WL 993473, at *3 (Tex. App.-San Antonio Mar. 15, 2017, no pet.) (mem. op.) (recognizing the holding in *Wasson Interests, Ltd.* as extending the proprietary-governmental dichotomy to contract claims).

Following remand after *Wasson*, the lower courts again ruled that the City enjoyed immunity on the breach of contract claim. The Texas Supreme Court recently reversed in *Wasson v. City of Jacksonville,* No. 17-0198, 2018 WL 2441894 (Tex. June 1, 2018). "[T]o

determine whether governmental immunity applies to a breach-of-contract claim against a municipality, the proper inquiry is whether the municipality was engaged in a governmental or proprietary function when it entered the contract, not when it allegedly breached that contract." The focus belongs on the nature of the contract, not the nature of the breach. If a municipality contracts in its proprietary capacity but later breaches that contract for governmental reasons, immunity does not apply. *Id.* "Conversely, if a municipality contracts in its governmental capacity but breaches that contract for proprietary reasons, immunity does apply. *Id.* at 5.

The distinction between a municipality's governmental and proprietary functions seems plain enough, but the rub comes when it is sought to apply the test to a given state of facts." *Id.* at *2 (internal quotation omitted). Texas appellate courts continue to struggle with the immunity concept.

B. Development Agreements

An economic development agreement was at issue on *City of Lancaster v. White Rock Commercial, LLC* 2018 Tex. App. LEXIS 10750 (Tex. App. —Dallas, 2018, no pet.). In 2007 White Rock entered into two contracts with the City pursuant to Chapter 380. In both contracts the City was required to provide economic incentives to White Rock for agreeing to design and construct infrastructural improvements for a 1.4 million square foot industrial park. To receive certain payments White Rock was required to construct a 440,000 square foot industrial building.

After the City refused to make some of the reimbursements, White Rock sold the building at a loss and its lender took the undeveloped remainder of the property through a deed in lieu of foreclosure. White Rock sued for breach of contract, and won a multi-million dollar award at trial.

The City argued that its actions in entering into the 380 Agreement were governmental rather than proprietary. Because the functions included street construction, sanitary sewer, water lines, etc. the court of appeals concluded they were governmental functions.

A breach of a development agreement was similarly addressed in *CHW – Lattas Creek, L.P. v. City of Alice*, 2018 Tex. App. LEXIS 8888 (Tex. App. — San Antonio 2018, pet filed). CHW entered into a Chapter 380 Agreement to facilitate the construction of a multi-use complex and to facilitate the construction of a hotel. CHW conveyed certain property to the City to effectuate the economic development project.

The agreement provided the conveyance was contingent upon: (1) the City completing construction of an aquatic center within thirty-six months; and (2) substantially completing an amphitheater as described in a master plan on file with the City's secretary. Absent substantial completion of those structures, all or a portion of the purchased property was subject to be re-conveyed to CHW at the same per acre price paid by the City. Similarly, although the City was only required to facilitate the construction of a hotel by a third party, if the hotel was not constructed, CHW was granted a right of first refusal to purchase the lot or lots on which the hotel was to be constructed in the event the City sought to sell the lot or lots. The park property was limited to use as a city park but was not subject to re-conveyance.

In the development agreement, CHW and the City agreed the conveyed property would be developed in phases. With respect to the City utility improvements, the City agreed to extend water lines and sanitary sewer mains from their existing termination points to other points that would facilitate the development of the developer property. With respect to the road improvements, the City agreed to construct two roads to facilitate the development. CHW and the City agreed to work together to develop a schedule for each phase of the construction, and the City agreed to commence construction of the aquatic center, utility improvements, and City road improvements within 120 days after the closing on the purchased property.

The parties expressly agreed that the agreement was made and subject to the requirements of Tex. Loc. Gov't Code Ann. Chapter 271, Subchapter 1 the City expressly waived sovereign immunity to suit for the purpose of adjudicating a claim for breach of contract. About four years later CHW sued the City because the City had not constructed sufficient infrastructure and failed to construct the amphitheater. The City argued immunity in its plea to the jurisdiction.

CHW argued that the City was engaged in a proprietary function when it entered into the development agreement. The list of governmental factors in the Texas Torts Claims Act includes "community development or urban renewal activities undertaken by municipalities and authorized under Chapters 373 and 374, Local Government Code." Tex. Civ. Prac. & Rem. Code § 101.6215(34). Although CHW argued that its community development activities were pursuant to Chapter 380, the Court took a broad view and concluded that this development under Chapter 380 was a governmental function.

A different result was reached in *City of Westworth Village v. City of White Settlement*, 558 S.W.3d 232 (Tex. App.-Fort Worth 2018, pet. den.). The two cities negotiated an economic development plan to locate a Walmart and Sam's store on a tract located in both cities. This led to an increase in Westworth Village's retail sales tax revenue, some of which were payable to White Settlement. Twelve years later Westworth Village notified White Settlement of its decision to terminate the agreement. White Settlement filed for breach of contract.

In response to Westworth Village's plea to the jurisdiction, the Fort Worth Court of Appeals found the agreement to be proprietary in nature. *Id*. at 235. The court reviewed the list of governmental functions listed in the Texas Torts Claim Act and noted that an argument could be made that the function of the Agreement was "tax collection." However, tax collection only came into play as a basis for calculating the periodic payments due under the Agreement. *Id*. at 243.

Applying the *Wasson* test, the court of appeals found that (1) Westworth Village's act of entering into the contract was discretionary and not ministered; (2) the contract was intended to benefit Westworth Village's residents rather than the general public; (3) Westworth Village acted on its own, rather than the states behalf; and (4) the contract was not sufficiently related to a governmental function so as to render the act more governmental rather than proprietary. *Id*. at 244. Applying *Wasson II*, the court concluded that the 380 agreement only "touched" on taxation and planning. *Id*. at 250. The agreement's primary purpose was to foster local economic development.

C. *Trinity v. City of Dallas*

The Dallas Court of Appeals also addressed the Dichotomy in *City of Dallas v. Trinity East Energy LLC*, 05-16-00349-CV (Tex. App.—Dallas, Feb. 7, 2017, pet. denied) where the City of Dallas accepted nearly $20,000,000.00 from Trinity in bonus payments for oil and gas leases covering city-owned land. But the City ultimately denied Trinity the ability to explore the minerals covered by the leases by refusing to approve the necessary city permits to drill on either public or private property. Following Trinity East filing suit, the City filed a plea to the jurisdiction. The trial court denied the plea as to Trinity's regulatory takings claim but granted the plea as to Trinity's breach of contract fraud and related torts claim.

Trinity then began the lengthy, costly, and necessary process of engineering and planning activities, designing a system of drillsites, roads, and pipelines to allow the drilling and production of the minerals. Trinity spent over $450,000 on engineering, surveys, consultants, planning, environmental testing, and other matters required for the SUP applications, which it submitted in March and April 2011 in accordance with the Dallas Drilling Ordinance.

Disregarding the City's lease obligations and the staff recommendations of approval, the City Plan Commission ("CPC") recommended denial of the SUPs by a 9-to-6 vote. Per City ordinance, Trinity appealed the CPC's decision to the City Council. Due to the CPC denial, a super-majority (3/4ths vote) of the City Council was required to approve the SUP Applications and allow Trinity the right to drill for which Trinity had long ago paid the City $20,000,000. In August 2013, and ignoring its contractual obligations, the Council denied the appeals with only a simple majority voting to approve the SUP Applications.

Following the denial, Trinity brought suit against the City for breach of contract, inverse condemnation, declaratory judgment, and various intentional torts. The City filed a plea to the jurisdiction asserting immunity against all of Trinity's claims. A Dallas County district court ruled in favor of the City for all claims except Trinity's inverse condemnation claims. Both parties appealed to the Fifth District Court of Appeals. In a memorandum opinion published in February 2017, the Court of Appeals reversed in part and affirmed in part the trial court's ruling, holding that the City was *not* immune from *any* of Trinity's claim. The Texas Supreme Court denied the City's petition for review.

V. Contracts Under Chapter 271

A contract dispute with a municipality should first be analyzed in accordance with the Dichotomy principle. If the contract involves a proprietary function, then the merits should be evaluated similar to other private party litigation. For governmental functions, on the other hand, case law requires that the Legislature pass a statute waiving immunity.

Chapter 271 of the Texas Local Government Code, for example, provides that a local governmental entity that enters into a "written contract stating the essential terms of the agreement for providing goods or services to the local governmental entity" waives sovereign immunity to suit for the purpose of adjudicating a claim for breach of contract. Tex. Loc. Gov't Code Ann. §§ 271.151(2)(A); 271.152 (West 2016). Under Chapter 271, "goods or services" are generally construed broadly so as to encompass a wide array of activities. *Kirby Lake Dev., Ltd.*

v. Clear Lake City Water Auth., 320 S.W.3d 829, 839 (Tex. 2010). A service "includes generally any act performed for the benefit of another under some arrangement or agreement whereby such act was to have been performed." *Id.* A contract may fall under Chapter 271 even if the services provided were not the primary purpose of the agreement. *Id*.; *see also Lubbock County Water Control v. Church & Akin, LLC*, 442 S.W.3d 297, 301 (Tex. 2014). In addition, "a contractual relationship can include both the granting of a property interest and an agreement to provide goods or services." *Lubbock County Water Control* at 302 (citing *Coinmarch Corp. v. Aspenwood Apt. Corp*., 417 S.W.3d 909, 925 (Tex. 2013)) (emphasis in original).

A. Real Estate Contracts

Contracts that merely convey real property are not considered "good or services." In *Dallas Area Rapid Transit* ("DART") the court found that the contracts included an agreement for services to the governmental entity and that section 271.152's waiver of immunity from suit was applicable. *Dallas Area Rapid Transit v. Monroe Shop Partners, Ltd.,* 293 S.W.3d 839, 841 (Tex.App.—Dallas 2009, pet. denied). In *DART*, the contract at issue established that DART would sell, and Monroe would purchase and develop certain historically significant property near a rail station. 293 S.W.3d at 840. DART terminated the contract when Monroe allegedly failed to obtain the financing required by the contract. *Id.* Monroe sued DART for breach of contract, but DART filed a plea to the jurisdiction based on governmental immunity. *Id.* Monroe contended that DART's immunity was waived under section 271.152. *Id*. DART argued that section 271.152 was not applicable because the contract at issue was for the sale of real estate and not one for goods or services. *Id.* at 841. The Dallas Court of Appeals disagreed and found that the contract included promises by Monroe to provide certain pre-closing and post-closing development services to DART. *Id*. DART argued that the development services in the contract were not for its benefit but for the benefit of the State of Texas as it was the State and not DART that had restricted the use of the historic property. *Id.* The Dallas Court of Appeals disagreed and concluded that DART and the State were not mutually exclusive in this context. *Id.* The court explained that the contract required Monroe to accept an assignment of DART's responsibilities and restrictions in dealing with the historical nature of the property; get approval from DART on all construction documents related to the renovations; agree that all construction documents would belong to DART; obtain approval from DART on the construction company used by Monroe for the renovations; and perform a list of the specific construction work attached to the contract. *Id*. The court concluded that because of the agreement for these services, the contract was subject to the waiver of immunity under section 271.152. *Id.*

B. Development Agreements

In *Kirby Lake Development, Ltd. v. Clear Lake City Water Authority*, a number of developers entered into agreements with the Clear Lake Water Authority. 320 S.W.3d at 832. The agreements required the developers to build water and sewer facilities and to lease the facilities to the Water Authority free of charge. *Id*. The Texas Supreme Court held that the agreements provided for services under Chapter 271, noting that the developers "contracted to construct, develop, lease, and bear all risk of loss or damage to the facilities . . . ." *Id*. at 839.

The city pled immunity to the enforcement of a "Treated Wastewater Effluent Purchase Agreement" in *City of Merkel v. Copeland*, 561 S.W.3d 720 (Tex. App — Eastland 2018, pet.

filed). The Tin Cup Golf Course agreed to accept 100% of the City's wastewater and to pay the City $1.50/100,000 gallons. Several years later the City turned off the spigot because the water did not meet minimum TCEQ quality standards. Tin Cup was forced to convert to a 9 hole course and membership and profits declined.

Merkel filed a plea to the jurisdiction based upon immunity. First, the Court of Appeals held that the transaction was for a governmental function. The Texas Torts Claims Act includes sanitary sewer and sewer service as governmental functions. According to the Court, "the disposal of treated wastewater in some manner is essential to the City's operation of a wastewater treatment facility." *Id.* at 724.

Second, the court held that the contract was not an agreement for providing goods or services to the City as provided for in § 271.151(2)(A). The only services being provided under the contract were provided by the City to the golf course and not vice versa.

The Chapter 271 issue was also addressed in *CHW – Lattas Creek, L.P. v. City of Alice*, 2018 Tex. App. LEXIS 8888 (Tex. App. — San Antonio 2018, pet filed). With respect to the § 271.152 waiver the court of appeals focused on the term "services". While CHW and the City agreed to undertake various activities to develop the CHW property, the development agreement did not obligate CHW to provide any services to the City. Even though the parties expressly stated in the Development Agreement that it was a written contract for providing goods and services to the City," recitals cannot be used to contradict the operative terms of a contract."

CHW next argued that immunity was expressly waived in the development agreement. The court of appeals held that the City still should not be estopped from raising the immunity defense: "Although we do not condone the actions by the city officials in agreeing to the inclusion of the immunity waiver in the Development Agreement, we hold the facts in this case do not present an exceptional case for estopping the City." Basically, the court believed that CHW should have known the law and somehow negotiated an agreement in which they would be required to provide services.

The Dallas Court of Appeals held that a governmental function was involved in *City of Lancaster v. White Rock Commercial*. With respect to the Chapter 271 claim the City argued in City of Lancaster that the 380 Agreement was not subject to the statute because it lacked an essential term (time of performance) and did not relate to the provision of goods and services. The court of appeals concluded that the law implied a reasonable time for White Rock to complete its contractual obligations. 2018 Tex. App. LEXIS 10750. *Id*. at 13.

The court of appeals then considered whether the 380 Agreement was for the provision of "goods and services" under Chapter 271. Lancaster argued that White Rock would have been required to construct the infrastructure described in the 380 Agreement pursuant to the City's subdivision ordinance. It relied upon appellate opinions holding that the benefit to the City was too attenuated to fit within the statute. *Id.* at 14. In fact, the 380 Agreement expressly stated that it would benefit the City by growing its economy.

However, the court held that the provision of infrastructure improvements was itself a direct benefit to the City. The City's agreement to pay White Rock for such construction was

further evidence of a contract for services. Lancaster was ordered to pay White Rock the full amount of its infrastructure construction costs.

CONCLUSION

While the Legislature and the Supreme Court have reduced the breadth of the immunity defense during the last few years, immunity remains most cities' first line of defense against contract enforcement.