

Contract Immunity Update

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For the 2016 TCAA conference, I provided an update of three important Texas Supreme Court cases regarding contractual immunity¹—*Lubbock Cnty. Water Control & Improvement Dist. v. Church & Akin, L.L.C.*, 442 S.W.3d 297 (Tex. 2014); *Zachry Const. Corp. v. Port of Houston Auth. of Harris Cnty.*, 449 S.W.3d 98 (Tex. 2014); and *Wasson Interests, Ltd. v. City of Jacksonville*, 2016 WL 1267697 (Tex. Apr. 1, 2016).

Since last year’s conference, the Texas Supreme Court has not issued any further decisions on the issue. Instead, most of the case law developments have been from the courts of appeals as they attempt to interpret and apply the *Zachry* and *Wasson* decisions. This paper is an update of my 2016 paper, which summarized each of the three Texas Supreme Court cases listed above. As you will see, I have left the original text intact and added “UPDATE” sections with the latest significant opinions applying and discussing the Supreme Court’s decisions.

1. **Chapter 271 waives immunity only if the plaintiff was required to provide goods or services directly to the governmental entity.**

Lubbock Cnty. Water Control & Improvement Dist. v. Church & Akin, L.L.C., 442 S.W.3d 297 (Tex. 2014).

Opinion by Justice Boyd, joined by Justices Hecht, Green, Guzman, Lehrmann, Devine, and Brown. Dissent by Justice Willett, joined by Justice Johnson.

Chapter 271 waives immunity for a breach of contract claim based on a contract for “providing goods or services to [a] local governmental entity.” Tex. Loc. Gov’t Code § 271.151-.152. Prior to 2014, the Texas Supreme Court and lower courts had interpreted the requirement that the contract involve the provision of goods or services to the government fairly liberally.

For example, in *Ben Bolt–Palito Blanco Consol. Indep. Sch. Dist. v. Tex. Political Subdivisions Prop./Cas. Joint Self Ins. Fund*, 212 S.W.3d 320, 327 (Tex. 2006) the Supreme Court held that a governmental entity (the Fund) could be sued for claims arising from a contract under which the Fund was **providing** insurance services to its members. In other words, the provision of services was **by**, not **to**, the governmental entity being sued. *Id.* According to the Court, the Fund’s members could sue the Fund because the members had contractually agreed to elect a board of directors and to participate in the resolution of claim disputes. *Id.* In short, if **any services** were being provided to the governmental entity, then immunity was waived for all breach claims arising from the contract.

¹ The Chapter 271 waiver refers to sections 271.151-271.158 of the Texas Local Government Code, which waives governmental immunity for certain breach-of-contract claims

After *Ben Bolt*, it seemed that almost any contract could be construed as providing some service to the governmental entity. Not so. In *Lubbock County*, the Court established limits on what activities constitute a service to a governmental entity. See *Lubbock Cnty. Water Control & Improvement Dist. v. Church & Akin, L.L.C.*, 442 S.W.3d 297, 303-308 (Tex. 2014). In that case, the plaintiff—Church & Akin—was leasing the Buffalo Springs Lake marina from Lubbock County WCID and had committed not to use the property for any other purpose. *Id.* at 303- 304. It also agreed that it would issue catering tickets that could be redeemed at the gate for admittance to the lake. *Id.* at 305. Church & Akin argued that it was providing a service to the WCID by operating the marina and issuing catering tickets. *Id.* at 302, 305. The Court disagreed. *Id.* at 305.

According to the Court, operation of marina service was not a service to the WCID for at least two reasons. *Id.* at 302-305. First, the lease did not *require* Church & Akin to operate a marina; it simply restricted them from using the property for another purpose. *Id.* at 303. As such, the WCID had no right to receive marina service. *Id.* The mere fact that marina service might result from the lease did not make the lease an agreement to provide services to the WCID. *Id.* Second, even if the lease had required Church & Akin to use the property as a marina, it would have been providing marina services to the individuals using the marina and not to the WCID. *Id.* at 303-304.

The Court reached a similar conclusion with respect to the catering tickets. Church & Akin’s promise that it “will issue catering tickets” was not a commitment to provide a service, but only an acknowledgement that it intended to and could issue marina tickets for the benefit of its business. *Id.* at 305.

Practice Points

Lubbock County sets the precedent for courts to take a hard look at activities a plaintiff claims constitute a service to a governmental entity. When reviewing leases, real estate transactions, and other contracts where the governmental entity is providing the primary good or service, it is important to consider whether the governmental entity should require anything beyond monetary payment in return. Each contractual obligation or requirement of the other party creates a potential basis for smart attorneys to argue that the contract included the provision of a good or service to the governmental entity. If the governmental entity wants or needs to control the other party’s conduct, it should do so through restrictions rather than requirements, to the extent possible.

2. Chapter 271’s limit on recoverable damages defines when immunity is waived, but recoverable damages include all direct damages that are payable and unpaid under contract law rather than what is due and owing under the contract.

Zachry Const. Corp. v. Port of Houston Auth. of Harris Cnty., 449 S.W.3d 98 (Tex. 2014).

Opinion by Justice Hecht, joined by Justices Green, Guzman, Devine, and Brown. Dissenting opinion Justice Boyd, joined by Justices Johnson, Willett, and Lehrmann.

In *Zachry Construction* the Texas Supreme Court held that immunity was waived for a claim for delay damages even though such damages were disclaimed—and thus arguably not “due and owing”—under the contract at issue. *Zachry Const. Corp. v. Port of Houston Auth. of Harris Cnty.*, 449 S.W.3d 98, 106 (Tex. 2014). *Zachry* arose from the construction of a wharf for the Port of Houston Authority. *Id.* at 101-102. In the parties’ contract, *Zachry* (the contractor) agreed that it would not be entitled to damages caused by delay, even if the delay was caused in whole or in part by “the negligence, breach of contract or other fault of the Port.” *Id.* at 103. After the project was significantly delayed, *Zachry* sued for delay costs allegedly caused by the Port’s intentional interference with construction. *Id.* The case raised two important questions: First, did the Chapter 271 waiver apply to *Zachry*’s claim so that immunity was waived? *Id.* at 106. Second, was the no-damages-for-delay provision enforceable if the delay was caused by the Port’s intentional misconduct? *Id.* at 115.

In deciding whether immunity was waived, the Court first considered whether § 271.153 of Chapter 271, which limits recoverable damages, “define[s] and restrict[s] the scope of the waiver of immunity.” *Id.* at 106. To answer that question, the Court examined the waiver language in § 271.152:

A local governmental entity that is authorized by statute or the constitution to enter into a contract and that enters into a contract subject to this subchapter waives sovereign immunity to suit for the purpose of adjudicating a claim for breach of the contract, ***subject to the terms and conditions of this subchapter.***

Id. (quoting Tex. Loc. Gov’t Code § 271.152). According to the Court, the “subject-to-the-terms-and-conditions” phrase incorporates the other nine sections of the Chapter 271 waiver to define the waiver’s scope. *Id.* The Court further noted that it had applied this interpretation in *Tooke v. City of Mexia* when it concluded that immunity was not waived for the *Tooke*’s lost profits claim—damages that are expressly prohibited under § 271.153. *Id.* at 108. Despite the rather straightforward analysis in

Tooke, the Supreme Court's later decision in *Kirby Lake Development, Ltd. v. Clear Lake City Water Authority* led some courts of appeals to conclude that immunity could be waived regardless of what damages were claimed. *Id.* at 108-109. That conclusion was wrong. *Id.* at 109. The Court clarified that the governmental entity in Kirby Lake was arguing that there were no recoverable damages **because** there was **no liability**. *Id.* at 109-109. The purpose of § 271.153 is to limit the amount of damages once liability has been established, not to foreclose a party's ability to seek a determination of whether liability exists. *Id.* at 109. As such, § 271.153 prohibits waiver only when a party seeks damages that are not recoverable **even if** the governmental entity is liable. *Id.* The entire Court joined in this holding. *Id.* at 109, 120 n. 1.

In light of this interpretation, the Court then had to decide whether the delay damages Zachry sought were permitted by the Act. *See id.* at 106. Section 271.153 allows a party to recover “the balance due and owed . . . under the contract, including any amount owed as compensation for the increased cost to perform the work as a direct result of owner-caused delays.” Tex. Loc. Gov't Code § 271.153(a)(1). The Port argued that no balance could be due and owed to Zachry because the contract did not expressly provide for the payment of delay damages. *Zachry*, 449 S.W.3d at 111. The majority of the Court rejected this argument, holding that § 271.153 did not require the “balance due and owed . . . under the contract” to be ascertainable from the contract. *Id.* Instead, it interpreted the balance due and owed to mean the amount of damages for breach of contract that were payable and unpaid under the common law. *Id.* In other words, all damages generally available under normal contract law principals are recoverable unless expressly prohibited by § 271.153 (e.g., lost profits), regardless of whether such damages are provided for in the contract. *Id.* at 111-12. Perhaps most importantly, in determining whether immunity had been waived, the Court did not consider the fact that Zachry had expressly agreed that it would not be entitled to delay damages—or stated differently, that Zachary had agreed delay damages would not be “due and owed . . . under the contract.” *See id.* at 111-14.

Practice Points

Zachry is a tough case for cities. It begins with a very positive holding—immunity is not waived if recoverable damages are not pled. But then it takes a pretty big leap in the opposite direction by deciding that amounts due and owing means all common-law contract damages rather than the damages the parties expressly agreed to in the contract. The likely result is that immunity will be found to be waived for most contract claims regardless of what damage limitations cities include in their contracts. The one exception may be lost profits, which were found to be barred in *Tooke*. *Tooke v. City of Mexia*, 197 S.W.3d 325, 346 (Tex. 2006). But as the dissent points out, even this has

been called into question:

In *Tooke*, the Court held that the claimants could not recover . . . because they claim[ed] only lost profits on additional work they should have been given, which are consequential damages excluded from recovery under the statute . . . If, as the Court holds today, a balance due and owed . . . under the contract is simply the amount of damages for breach of contract payable and unpaid, . . . the Tookes should have been able to recover lost profits under section 271.153(a)(1), and they should not have been excluded as consequential damages under subsection (b)(1) because they fall within the exception for consequential damages expressly authorized under subsection (a)(1).

Zachry, 442 S.W.3d at 126-27. Of course, this doesn't mean cities should give up on contractual provisions limiting their liability. Those limitations can still protect a city from ultimately having to pay certain damages. But unfortunately, they won't necessarily help a city avoid the costs associated with being forced to participate in litigation in the first place.

It may be that all hope on this issue isn't lost just yet. *Zachry* was a factually unique case. The jury found the Port had intentionally caused delay, and the Court refused to enforce a contractual provision. Further, delay damages are expressly allowed under § 271.153(a)(1). In a more recent case, the Fort Worth court of appeals has distinguished *Zachry* for those reasons and held that immunity was not waived for a breach of contract claim seeking additional employment benefits that were expressly barred by contract. *City of Colleyville v. Newman*, No. 02-15-00017-CV, 2016 WL 1314470 (Tex. App.—Fort Worth Mar. 31, 2016, pet. filed). A petition for review has been filed, presenting an opportunity for the Supreme Court to “clarify” the *Zachry* decision in a manner that grants greater meaning to the “under the contract” language in Chapter 271.

UPDATE

Since *Zachry*, four courts of appeals have issued opinions on whether certain amounts were due and owed under the contract so that immunity was waived. *Romulus Grp., Inc. v. City of Dallas*, No. 05-16-00088-CV, 2017 WL 1684631, at **4-5; *Cnty of Galveston v. Triple B. Servs., LLP*, 498 S.W.3d 176, 185-86 (Tex. App.—Houston [1st Dist.] 2016, pet. filed); *City of San Antonio v. Casey Indus., Inc.*, 2016 WL 320504, at **2-4 (Tex. App.—San Antonio Jan. 27, 2016, pet. denied); *City of Colleyville v. Newman*, 2016 WL 1314470, at **2-5 (Tex. App.—Fort Worth Mar. 31, 2016, pet. denied). All four courts seem unconvinced that the contract at issue does not factor into making that

decision.

In *County of Galveston v. Triple B Services*, the First Court of Appeals in Houston considered whether a county's immunity was waived for a claim for disruption damages. *Triple B. Servs.*, 498 S.W.3d at 181. The court's analysis of "under the contract" recognized that under *Zachry* the plaintiff could defeat immunity simply by alleging "any damages 'for the increased cost to perform the work as a direct result of the [County's] delays . . .' regardless of whether those damages are expressly addressed in the contract." *Id.* at 186. Yet the court still went on to consider whether the contract actually provided for at least some of the damages being claimed. *Id.* After concluding that it did, the court determined that immunity did not bar suit because "at least some damages . . . fit both under the contract at issue and "under the contract" as interpreted by *Zachry*." *Id.*

City of San Antonio v. Casey Industrial, Inc. is very similar. *Casey*, 2016 WL 320504, at **2-4. There, Casey sought additional compensation under the specific force majeure clause in its contract. *Id.*, at *2. Like the court in *Triple B*, the San Antonio Court of Appeals cited *Zachry's* holding that § 271.153 does not require the balance due and owed under the contract to be ascertainable from the contract. *Id.* It then considered whether the plaintiff, Casey, had provided any evidentiary support for its allegation that it was seeking "damages due and owed under the contract as 'the necessary and usual result' of [San Antonio's] wrongful refusal to pay Casey for its 'Claims' under the contract . . ." *Id.* In doing so, it did *not* discuss whether the damages sought were payable and unpaid under general contract law principles. *Id.*, at **2-3. Instead, it reviewed "unique" provisions in the contract at issue, and determined a specific contract clause provided a method for establishing amounts due and owed under the contract so that immunity was waived.

In *Romulus Group, Inc. v. City of Dallas*, the Dallas Court of Appeals did not even consider whether the damages sought would be available under normal contract law principals as stated in *Zachry*. No. 05-16-00088-CV, 2017 WL 1684631, at *4 (Tex. App.—Dallas May 2, 2017, no pet. h.). There, Romulus sought to recover hourly wages it claimed it was owed for temporary clerical and professional labor it had provided. *Id.*, at **1-2. Under the terms of its contract, the City had agreed to pay certain hourly rates for twenty-five different categories of employees supplied by Romulus. *Id.*, at *1. At some point, the City redesignated certain employees into a non-contractual category termed "Clerical Positions Not Listed" and paid Romulus a markup fee instead of the contractually agreed hourly rate. *Id.* Because the markup fee was less than the hourly rate, Romulus sued the city for the difference. *Id.* The City alleged that it was immune from suit because the labor for "Clerical Positions Not Listed" was extra-contractual, and thus no amounts were due and owing under the contract. *Id.*, at **1-2. Romulus

disagreed, arguing that its claim fell within the scope of the contract. *Id.* In resolving the claim in favor of Romulus, the Court made no mention of the Supreme Court’s *Zachry* standard for amounts due and owing, focusing instead solely on the fact that the claim fell within the terms of the contract. *Id.*, at **3-5.

Finally, the Fort Worth Court of Appeals has gone one step further by distinguishing *Zachry*. *Colleyville*, 2016 WL 1314470, at **4-5. In *City of Colleyville v. Newman*, a municipal court judge hired as an independent contractor sued the city after the IRS ruled he should have been classified as an employee. *Id.*, at *1. Specifically, the judge claimed that under *Zachry*, certain benefits offered in writing to employees of the city, such as vacation pay and health insurance, were amounts “due and owed” under his contract with the city. *Id.*, at *4. The court disagreed, distinguishing *Zachry* on two grounds. *Id.*, at **4-5. First, in *Zachry* the delay damages sought were expressly allowed under the waiver statute. *Id.*, at *4. Second, the *Zachry* court invalidated the no-damages-for-delay clause that would have precluded delay damages from being owed under the contract. *Id.* According to the court, the judge’s claim was different because his agreement expressly barred recovery of any additional benefits or compensation beyond what had already been paid, and no reason existed to void that provision. *Id.*, at *5. “Thus, there is no balance ‘due and owed’ by the Cities under the agreement.” *Id.* While the Court’s decision makes sense under the plain language of § 271.153, it does not square with *Zachry*, which ignored a contractual disclaimer of damages in deciding whether immunity was waived.

3. Governmental immunity does not apply to bar contract-related claims when a city acts in its proprietary capacity.

Wasson Interests, Ltd. v. City of Jacksonville, 2016 WL 1267697 (Tex. Apr. 1, 2016).

Opinion by Justice Brown, joined by all Justices except Justice Devine (not participating).

Two years ago, I wrote and spoke about the issues decided in *Wasson*—issues I had briefed in other cases that were ultimately settled. The underlying law on the governmental-proprietary dichotomy dates back over 100 years and is worth reviewing for context before discussing the *Wasson* decision.

Background/History

In 1884, the Texas Supreme Court carved out an exception to the general rule that cities enjoy governmental immunity from all lawsuits. *City of Galveston v. Posnainsky*, 62 Tex. 118, 131 (1884). For the first time, the Court recognized a distinction between a City’s governmental and proprietary functions and held that Galveston was not

immune from a tort claim based on its failure to maintain its sidewalks because such maintenance was a proprietary act. *Id.* When a city engages in a proprietary function, the Court explained, the city is treated as a private actor:

In so far, however, as [cities] exercise powers, voluntarily assumed—powers intended for the private advantage and benefit of the locality and its inhabitants—there seems to be no sufficient reason why they should be relieved from that liability to suit and measure of actual damage to which an individual or private corporation exercising the same powers for a purpose essentially private would be liable.

Id. at 127. Over 100 years later, the Court again discussed the proprietary-governmental distinction. *Gates v. City of Dallas*, 704 S.W.2d 737, 739 (Tex. 1986). But, this time it did so in the context of a contract case. *Id.* After broadly stating that cities engaged in proprietary functions are subject to the same duties and liabilities as private persons, the Court held that Dallas was liable for attorney fees under the precursor statute to Chapter 37 of the Texas Civil Practice & Remedies Code. *Id.*

Although *Posnainsky* applied the governmental-proprietary distinction to a tort claim, a number of appellate courts extended the distinction to contract-related cases. *See City of Georgetown v. Lower Colo. River Auth.*, 413 S.W.3d 803, 810 n.4 (Tex. App.—Austin 2013, pet. withdrawn).² Most of these courts did so with little or no analysis, simply assuming that “the dichotomy applies with equal force to contract claims.” *See, e.g., City of Mexia v. Tooke*, 115 S.W.3d 618, 624-225 (Tex. App.—Waco 2003), *aff’d*, 197 S.W.3d 325 (Tex. 2006).

But in 2006 the Texas Supreme Court brought that assumption into question when it stated that the “proprietary-governmental dichotomy has been used to determine a municipality’s immunity from suit for tortious conduct . . . [b]ut we have never held that this distinction determine whether immunity from suit is waived for breach of contract claims . . .” *Tooke v. City of Mexia*, 197 S.W.3d 325, 343 (Tex. 2006).

² Citing *Bailey v. City of Austin*, 972 S.W.2d 180, 192-93 (Tex. App.—Austin 1998, pet. denied); *Temple v. City of Houston*, 189 S.W.3d 816, 819-820 (Tex. App.—Houston [1st Dist.] 2006, no pet.); *City of Roman Forest v. Stockman*, 141 S.W.3d 805, 811 (Tex. App.—Beaumont 2004, no pet.); *City of Mexia v. Tooke*, 115 S.W.3d 618, 624-25 (Tex. App.—Waco 2003), *aff’d*, 197 S.W.3d 325, 347 (Tex. 2006); *Williams v. City of Midland*, 932 S.W.2d 679, 683-84 (Tex. App.—El Paso 1996, no writ); *City of Houston v. Sw. Concrete Constr., Inc.*, 835 S.W.2d 728, 732-33 (Tex. App.—Houston [14th Dist.] 1992, writ denied); *City of Dallas v. Moreau*, 718 S.W.2d 776, 779-80 (Tex. App.—Corpus Christi 1986, writ ref’d n.r.e.); *Int’l Bank of Commerce of Laredo v. Union Nat’l Bank of Laredo*, 653 S.W.2d 539, 546 (Tex. App.—San Antonio 1983, writ ref’d n.r.e.); *Blythe v. City of Graham*, 287 S.W.2d 527, 530 (Tex. App.—Fort Worth 1956, writ ref’d n.r.e.); *Boiles v. City of Abilene*, 276 S.W.2d 922, 925 (Tex. App.—Eastland 1955, writ ref’d); *City of Crosbyton v. Tex.-N.M. Util. Co.*, 157 S.W.2d 418, 420-21 (Tex. App.—Amarillo 1941, writ ref’d w.o.m.); *Tex. One P’ship v. City of Dallas*, No. 05-92-01097-CV, 1993 WL 11621, at *3 (Tex. App.—Dallas Jan. 15, 1993, writ denied) (not designated for publication).

In support of that statement, the Court cited *Gates* with a “Cf.”³ signal. *Id.* It then explained that it did not need to decide whether the distinction applied to contracts because the contract in question involved a governmental function, and thus even if the distinction applied, the city had immunity. *Id.*

The Supreme Court’s statement in *Tooke* regarding the applicability of the governmental-proprietary distinction did not have much of an impact initially. Several courts of appeals continued applying the distinction to contract claims. *See, e.g., E. Houston Estate Apartments, L.L.C. v. City of Houston*, 294 S.W.3d 723, 731-32 (Tex. App.—Houston [1st Dist.] 2009, no pet.); *Smith v. City of Blanco*, No. 03-08-00784-CV, 2009 WL 3230836, at *3 (Tex. App.—Austin Oct. 8, 2009, no pet.) (mem. op.); *Casso v. City of McAllen*, No. 13-08-00618, 2009 WL 781863, at **5-7 (Tex. App.—Corpus Christi Mar. 26, 2009, pet. denied). Once again, they did so with virtually no analysis or discussion. *See id.* But then, the Fourth Court of Appeals decided *Wheelabrator. City of San Antonio v. Wheelabrator Air Pollution Control, Inc.*, 381 S.W.3d 597 (Tex. App.—San Antonio 2012, pet. denied). After conducting the most thorough analysis of the issue to date, the court determined that the governmental-proprietary distinction did not apply to contracts-related claims. *Id.* at 601-605. Instead, it was limited to torts. *See id.* at 605. Following that decision, five other courts of appeals decided the same issue. Only one—the Austin court of appeals—decided that immunity did not apply to bar contract claims arising from proprietary activities.

Wasson Opinion

Unfortunately for cities, the Texas Supreme Court sided with the Austin court of appeals, albeit perhaps for slightly different reasons. *See Wasson Interests, Ltd. v. City of Jacksonville*, No. 14-0645, 2016 WL 1267697, at *2 (Tex. Apr. 1, 2016). In *Wasson*, the Court held that immunity does not apply when a city acts in its proprietary capacity. *Id.* at *2, *9. The Court reached that conclusion because of the derivative nature of cities’ immunity. *Id.* at *9. Unlike the state, cities and other political subdivisions have no independent sovereignty. *Id.* Instead, all of their sovereignty—and by extension all of their immunity—is derived from the state. *Id.*

Thus, when a city performs an act mandated by the state for the benefit of the general public (referred to by the Court as “the people”), it acts under the state’s authority and enjoys the state’s immunity. *Id.* Conversely, when a city *chooses* to engage in an activity for the benefit of its citizens, “it ceases to derive its authority—and . . . its immunity—from the state’s sovereignty.” *Id.* at *7. Activities done under state mandate

³ Cf. means authority supports a proposition different from the main proposition but sufficiently analogous to lend support.

are governmental, while voluntary activities are proprietary. *Id.* at *4. In the Court’s opinion, proprietary activities were comparable to *ultra vires* actions in that neither are “done pursuant to the will of ‘the people,’” and so “protecting them via the state’s immunity is not an efficient way to ensure efficient allocation of state resources.” *Id.* at *7.

As part of its opinion, the Court also addressed many cities’ argument that the Legislature had not clearly and unambiguously waived immunity for contract-claims arising from proprietary functions because Chapter 271 was not limited to governmental contracts. *Id.* In fact, Chapter 271 does not mention the governmental-proprietary dichotomy at all. *See* Tex. Loc. Gov’t Code §§ 271.151-.158. In rejecting this argument, the Court announced a second important holding from the *Wasson* opinion. Although the Legislature is solely responsible for *waiving* immunity, courts decide whether immunity *exists* in the first place. *Wasson*, 2016 WL 1267697 at *3. At the time Chapter 271 was enacted, many courts had held that immunity did not bar a claim arising from a proprietary contract. *See id.* at *6. These opinions were sufficient to create “well-established” jurisprudence or common law, which the Legislature could only abrogate expressly—i.e., not by implication. *Id.* at **7-8. Chapter 271’s language did not meet this test: not only was the dichotomy not mentioned, but also § 271.158 states that the waiver was not intended to *create* immunity. *Id.* at *8.

The final issue addressed by the Court was application of the dichotomy in the contract context. After taking the position that the Legislature couldn’t alter the common law by implication, the Court described the Legislature’s definitions and list of proprietary and governmental activities for *torts* as guidance in classifying *contracts*. *Id.* at *9.

Practice Points

In the wake of *Wasson*, cities should assume that potential plaintiffs will make every effort to classify the activity underlying their claim as proprietary. Although the Tort Claims Act explicitly defines many activities, even the Supreme Court has admitted the classification of activities “is not always a cut-and-dried task.” *Id.* at *9. Whether or not a contract claim arose from a proprietary activity is likely to involve fact questions, making it more difficult for a city to have its plea to the jurisdiction decided at the outset of a case. The result: more litigation, involving more time and expense.

While some of the impacts of the *Wasson* decision may be unavoidable, cities can take steps to help protect taxpayer money from contract-related suits.

1. When entering into a contract, consider whether the contract involves or may involve a proprietary function.

The Court's decision to apply the TTCA list of functions may have been inconsistent with its own reasoning, but it's probably the best result for cities. In enacting that list, the Legislature changed the classification of many activities from proprietary to governmental, thereby broadening cities' immunity protections.

The TTCA list defines the following activities as governmental:

- | | |
|---|--|
| <input type="checkbox"/> Police and fire protection and control | <input type="checkbox"/> Recreational facilities, including pools, beaches, and marinas |
| <input type="checkbox"/> Health and sanitation services | <input type="checkbox"/> Vehicle and motor driven equipment maintenance |
| <input type="checkbox"/> Street construction and design | <input type="checkbox"/> Parking facilities |
| <input type="checkbox"/> Bridge construction and maintenance and street maintenance | <input type="checkbox"/> Tax collection |
| <input type="checkbox"/> Cemeteries and cemetery care | <input type="checkbox"/> Firework displays |
| <input type="checkbox"/> Garbage and solid waste removal, collection, and disposal | <input type="checkbox"/> Building codes and inspection |
| <input type="checkbox"/> Establishment and maintenance of jails | <input type="checkbox"/> Zoning, planning, and plat approval |
| <input type="checkbox"/> Hospitals | <input type="checkbox"/> Engineering functions |
| <input type="checkbox"/> Sanitary and storm sewers | <input type="checkbox"/> Maintenance of traffic signals, signs, and hazards |
| <input type="checkbox"/> Airports, including when used for space flight | <input type="checkbox"/> Water and sewer service |
| <input type="checkbox"/> Waterworks | <input type="checkbox"/> Animal control |
| <input type="checkbox"/> Repair garages | <input type="checkbox"/> Community development or urban renewal activities undertaken by municipalities and authorized under Chapters 373 and 374, Local Government Code |
| <input type="checkbox"/> Parks and zoos | <input type="checkbox"/> Latchkey programs conducted exclusively on a school campus under an interlocal agreement with the school district in which the school campus is located |
| <input type="checkbox"/> Museums | <input type="checkbox"/> Enforcement of land use restrictions under Subchapter E, Chapter 212, Local Government Code. |
| <input type="checkbox"/> Libraries and library maintenance | |
| <input type="checkbox"/> Civic, convention centers, or coliseums | |
| <input type="checkbox"/> Community, neighborhood, or senior citizen centers | |
| <input type="checkbox"/> Operation of emergency ambulance service | |
| <input type="checkbox"/> Dams and reservoirs | |
| <input type="checkbox"/> Warning signals | |
| <input type="checkbox"/> Regulation of traffic | |
| <input type="checkbox"/> Transportation systems | |

The listed proprietary functions are:

- Operation and maintenance of a public utility
- Amusements owned and operated by a city
- Any activity that is abnormally dangerous or ultrahazardous

Tex. Civ. Prac. & Rem. Code § 101.0215(a)-(b). Neither list is exclusive. *Id.* However, an activity that is listed as governmental cannot be proprietary. *Id.* at § 101.0215(c). Thus, although operation of a public utility is defined as proprietary, the operation of a water utility is governmental because it falls within the meaning of water and sewer service. *See* Tex. Civ. Prac. & Rem. Code § 101.0215(a)(32), (b)(1), (c).

Cities should think broadly in considering whether a contract will relate to a governmental or proprietary activity. This is especially important for contracts for common supplies (office supplies, gravel, fuel) or services (janitorial, legal, financial). If the contract appears to relate to a governmental function but contemplates performance over a period of time, think about whether and how the scope of the contract might change. If there might be a need to use the goods or services for a proprietary function in the future, consider treating the contract as proprietary now.

2. Try defining your contract as governmental.

Employ the old adage that “it never hurts to try.” Courts are likely going to be the final decider of whether a contract is governmental or proprietary. But it can’t hurt* to include a contractual provision defining the contract as governmental. Better yet, include the reasons why. If nothing else, such a provision is evidence of the parties’ intent.

* Every rule has its exception: Be very wary of agreeing that any contract involves a proprietary activity. This may seem obvious, but it’s amazing what parties will agree to just to get a deal done. If a city starts agreeing that activities are proprietary, it needs to be prepared to be stuck with that classification. It won’t want to be arguing that the governmental definition in one contract should govern, but the proprietary definition in another should not.

3. Consider separate contracts for governmental and proprietary activities.

Although it may seem like a hassle, cities may want to consider entering into two separate contracts with the same vendor—one that relates to proprietary activities and another that relates to governmental. This could be particularly helpful for long-term supply contracts. If the city discovers a better deal on light bulbs one year into a three-year contract, it could at least end the governmental-related contract early without fear of paying for future lost profits.

4. Insist on contractual limitations on liability.

Section 271.153 of the Texas Local Government Code limits the damages a plaintiff may recover from a city based on a breach of a goods or services contract. If immunity is not applicable to proprietary contracts, the statutory limitation would not apply. But, cities can still contractually limit their exposure. At the very least, cities can and should insist that they will not be liable for consequential damages, specifically lost profits. In the past, I recommended that this could easily be accomplished by stating

that damages will be limited to amounts recoverable under § 271.153 of the Texas Local Government Code. However, in light of the *Zachry* decision's broad interpretation of amounts due and owing, I believe it is much more prudent to spell out exactly what damages will and will not be allowed.

5. Use merger and written amendment clauses.

Proprietary-contract plaintiffs are not judicially and statutorily limited to claims based on written and properly authorized contracts. Instead, they can claim the parties agreed to additional terms, whether at the outset of the contract or by amendment somewhere down the line. To avoid factually-complicated disputes over the substance of the parties' agreement, include clauses that make clear that the contract contains the entire agreement (merger clause) and that amendments must be in writing and authorized by both parties (written amendment clause).

6. Train city employees to avoid entering into oral contracts.

In the proprietary context, oral and written representations, affirmations, and promises could all become the basis of a lawsuit (e.g., breach of an oral contract, promissory estoppel, or quantum meruit). Cities should ensure that employees—particularly those employees who participate in proprietary activities or are engaged in jobs that require a significant amount of interaction with contracts or citizen requests—understand the types of conduct that could create pseudo-contractual liability. Guidance on permissible assurances, what not to promise, proper methods of communication (i.e., in writing vs. orally), etc. can all go a long way to preventing a potential claim.

UPDATE

As predicted, *Wasson* appears to have led to an increase in the number of plaintiffs arguing that a City is not immune because it acted in its proprietary capacity. In just one year, four opinions on the subject have been issued;⁴ compare this to the four opinions on the *Zachry* amount-due-and-owing issue that were written in the past three years. Of these governmental-proprietary cases, two aptly demonstrate the inconsistency and lack of predictability created by application of the dichotomy to contract claims.

The first case is *Wasson*, which the Supreme Court remanded to the Tyler court of appeals. *Wasson Interests, Ltd. v. City of Jacksonville*, 513 S.W.3d 217, 219 (Tex. App.—

⁴ *Jamro Ltd. v. City of San Antonio*, No. 04-16-00307, 2017 WL 993473 (Tex. App.—San Antonio Mar. 15, 2017, no pet.); *City of San Antonio v. Hays Street Bridge Restoration Grp.*, No. 04-14-00886-CV, 2017 WL 776112 (Tex. App.—San Antonio Mar. 1, 2017, no pet. h.); *City of Dallas v. Trinity E. Energy, LLC*, No. 05-16-33249-CV, 2017 WL 491259 (Tex. App.—Dallas Feb. 7, 2017, pet. filed); *Wasson Interests, Ltd. v. City of Jacksonville*, 513 S.W.3d 217 (Tex. App.—Tyler 2016, pet. filed).

Tyler 2016, pet. filed). On remand, the Tyler court considered what capacity the City of Jacksonville had acted in when it terminated Wasson's lake lease. *Id.* at 221-23. Wasson argued that leasing lakefront lots for residential development was not listed activity under the definitions of governmental and proprietary functions in the Texas Tort Claims Act (TTCA). *See id.* at 222. As such, the Court must determine whether the city's action fit within the general definitions of governmental and proprietary activities in the TTCA. *See id.* Wasson urged the court to find that because the City's decision to lease the lots was discretionary, the City was acting in its proprietary capacity. *Id.* The City's arguments focused on the purpose of the lease and on the act that formed the basis of Wasson's claim—the lease termination. *See id.* According to the City, the lease and its terms were created for the development and maintenance of Lake Jacksonville, which was built to supply the City with water. *See id.* The lease was terminated as the result of the City's enforcement of its zoning ordinances, which were created for similar purposes. *See id.* The court sided with the City, holding that the City's actions fell within categories of actions listed as governmental—specifically, “waterworks,” “dams and reservoirs,” water and sewer service,” and “enforcement of land use restrictions.” *See id.*

Next and in contrast is *City of Dallas v. Trinity East Energy, LLC*, No. 05-16-00349, 2017 WL 491259 (Tex. App.—Dallas Feb. 7 2017, pet. filed). There, the City leased mineral rights on its property to Trinity for the purpose of drilling for oil and gas. *Id.*, at *1. During the negotiation process, Trinity advised the City that it would need to perform surface drilling at two specific sites in parkland and floodplain and asked for the City's pre-approval. *Id.* The City refused stating the process would take too long, but it did agree that the drill sites could be included in the leases and reassured Trinity that it would make approval of one site happen and use its best efforts to get approval of the other. *Id.*

After the leases were signed and Trinity had undertaken significant efforts to be prepared to drill, it applied to the City for drilling permits. *Id.*, at *2. The permits were ultimately denied, and following their denial the City adopted a new drilling ordinance with more restrictive setbacks that negated any possibility of Trinity locating a drill site on the leased properties. *Id.* Trinity sued. *Id.* Like Jacksonville, the City argued it had acted in a governmental capacity in entering into the leases and denying the permit applications, and thus it was immune. *Id.* at 3. Specifically, Dallas asserted in leasing the property it was engaged in the regulation of parks, floodplains, and building codes and inspections—listed governmental functions. *Id.* Similarly in denying Trinity's application, the City was enforcing land use restrictions, also a governmental function. *Id.*

Although Dallas' arguments bear striking resemblance to those made by the City

of Jacksonville—property leased for governmental purposes and frustrated by enforcement of zoning ordinances—the Dallas court of appeals reached the opposite result, concluding that the city had acted in its proprietary capacity because the leases would only benefit Dallas’ residents and not the public at large. *Id.*, at **3-4. The court relied, in part, on a 1956 Texas Supreme Court opinion, which held that a city could be estopped from cancelling mineral leases because such leases constituted a proprietary activity. *Id.* (citing *City of Corpus Christi v. Gregg*, 289 S.W.2d 746 (Tex. 1956)). In doing so, the court dismissed Dallas’ argument that *Gregg* had been decided prior to enactment of the TTCA, which reclassified many proprietary activities (e.g., regulation of parks) as governmental.

It is difficult to square the results in *Wasson* and *Trinity*. Both involved leases of city land for private use that would result in proceeds benefitting local citizens. Both also involved the cancellation or effective cancellation of the leases due to the enforcement of zoning rules. Perhaps the notable difference (at least based on the court’s opinions) is the apparent “fair factor.” *Wasson* had paid money but at least gotten to enjoy the benefits of his leases up to their termination. *Trinity* appears to have paid the City and expended considerable money for virtually no reward.

Of course, fairness is in the eye of the beholder. Fair or not, the *Wasson* and *Trinity* opinions demonstrate that the governmental-proprietary dichotomy creates not only fact issues but also judicial discretion, which mean increased litigation and costs for cities.

UPDATE: A waiver of immunity for recovery of attorney’s fees may not create a right to attorney’s fees.

The Legislature has waived immunity for a claim for attorney’s fees from the state (claims over \$250,000 only), counties, and local governmental entities. *See* Civ. Prac. & Rem. Code § 114.004(a)(3); Loc. Gov’t Code §§ 262.007(b)(3), 271.153(a)(3). But, one court of appeals recently held that the waiver statutes do not serve as a substantive basis for recovery of attorney’s fees; they only allow a party to recover fees “if another statute—or the contract—allows attorney’s fees.” *Triple B*, 498 S.W.3d at 189. In reality, no other statute provides a substantive basis for recovery of attorney’s fees on a breach-of-contract claim. Section 38.001 of the Civil Practice and Remedies Code, which permits fees in breach of contract cases against individuals and corporations, does not apply to governmental entities. *Id.* (citing *City of Corinth v. NuRock Dev. Inc.*, 293 S.W.3d 360, 379 (Tex. App.—Fort Worth 2009, no pet)). Thus, under *Triple B* a party would only be able to recover attorney’s fees if expressly permitted by contract. While this rule is not widespread and has not been adopted or approved by the Texas Supreme Court, it provides a basis for cities to argue they are not liable for attorney’s fees for breach of

contract unless such fees were contractually agreed to.