

TESTIMONY ON HOUSE BILL 1537

House Political Subdivision Committee

February 6, 2025

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Chairman Longmuir and members of the House Political Subdivision Committee, my name is Daniel L. Gaustad and I am the City Attorney for the City of Grand Forks. I want to thank you for the opportunity to provide testimony and express the City of Grand Forks' support to HB 1537.

To provide some background, there exists a Federal statute (7 U.S.C. § 1926(b)) that provides certain protections against curtailment or limiting rural water services when the rural water district is indebted to a federal agency. Generally, the lender is a USDA entity. The protections under this federal statute only arise if the rural water district has a loan from a federal lending agency. These protections generally relate to situations when a city annexes an area that the rural water district provides water service or in a reasonable period of time could provide water service.

In 1997, N.D.C.C. § 6-09.4-22 was enacted and provides similar protections against curtailment of rural water services. As with the federal statute, the protections under N.D.C.C. § 6-09.4-22 only arise if the rural water district is indebted to state lender. Generally, the state lender is the Public Finance Authority or the Bank of North Dakota.

In recognition of these statutory provisions, back in the year 2000, the City of Grand Forks entered into an agreement with Grand Forks Trail Rural Water Users, Inc. and Agassiz Water Users District. The stated purpose of this Agreement was to address the provisions of both the federal statute (7 U.S.C. § 1926(b)) and the state statute (N.D.C.C. § 6-09.4-22), when City of Grand Forks annexed areas and provided water service to these annexed areas. The annexations were anticipated to occur given the impact of the 1997 flood that inundated the City of Grand Forks.

It took over a year to negotiate the 2000 Agreement and each of the parties were represented by attorneys.

The 2000 Agreement set out areas immediately surrounding the City of Grand Forks, and the number of existing customers and the maximum future capacity that Grand Forks Trail Rural Water Users stated they were either providing water service to, or could provide water service to in the future. The total number of existing and future capacity customers of Grand Forks Rural Water Users represented it had was 447.

The City of Grand Forks paid Grand Forks Traill Rural Water Users a total of \$261,893.10 when the 2000 Agreement was signed, which represented the amount to be paid under the payment methodology set out in this agreement for the City's purchase of a portion of the total 447 existing and future capacity customers identified in the 2000 Agreement. The payment calculation set out in the 2000 Agreement applied to future annexations as well.

Shortly after the 2000 Agreement was executed, Grand Forks Traill Rural Water Users, Inc. became a rural water district under N.D.C.C. ch. 61-35. Importantly, in its petition to the State Engineer to become a water district, Grand Forks Traill Rural Water Users, Inc. specially cited the fact it had entered into the 2000 Agreement with the City of Grand Forks. Even more significant, is that in its petition to the State Engineer, Grand Forks Traill Rural Water Users represented its geographic service area boundary and the State Engineer's Order adopted and set out this geographic service boundary area. None of the areas that are the subject of the 2000 Agreement are within Grand Forks Traill Rural Water Users geographic service area.

In 2018, Grand Forks Traill Rural Water Users then petitioned the State Engineer to allow for its merger with another rural water district. The State Engineer approved this merger and the merged rural water districts became East Central Regional Water District (referred to herein as "East Central"). Significantly, in the merger petition, East Central represented to the State Engineer the geographic boundary of its service area and the State Engineer's Order approving the merger adopted and set out this geographic service boundary area. Again, none of East Central's geographic service area included the areas that are the subject of the 2000 Agreement.

For 20+ years the parties operated under and performed the terms of the 2000 Agreement.

At time of the 2000 Agreement was entered into, Grand Forks Traill Rural Water Users was indebted to a USDA agency and the Bank of North Dakota. These loans were later been paid off. In fact, the \$261,893.10 amount the City of Grand Forks paid in 2000 was used to pay down USDA lender loans. Over the course two plus decades of the 2000 Agreement, Grand Forks Traill Rural Water Users, and then East Central continued to get loans from state agencies – primarily through the Public Finance Authority.

Under N.D.C.C. § 6-09.4-22(2), agreements, like the 2000 Agreement, are allowed to be entered into, but if the rural water provider is indebted to a state lender, then the state lending entity is to be a party to the agreement. Also, N.D.C.C. § 6-09.4-22(2) provides that if the state lender is not a party, the agreement is deemed to be "invalid and unenforceable." Having the lender as a party to the agreement is not required under the Federal Statute (7 U.S.C. § 1926(b)). Nonetheless, concurrence by the USDA lender was secured regarding the 2000 Agreement. However, the Bank of North Dakota was not a party to the 2000 Agreement.

In November, 2020, East Central, the successor entity of Grand Forks Traill Rural Water Users, brought a lawsuit in Federal Court against the City of Grand Forks claiming the 2000 Agreement was void, *ab initio*, or from the very beginning, because the Bank of North Dakota was not a party to the 2000 Agreement – and even though the Bank of North Dakota was not a lender to East Central and had not been for years.

East Central in this lawsuit also claimed the City of Grand Forks was in violation of both 7 U.S.C. § 1926(b) and N.D.C.C. § 6-09.4-22, by “curtailing” its ability to provide water service 130+ subdivisions that are now part of the City. In fact, one of the subdivisions East Central is claiming to have been curtailed contains the City of Grand Forks’ new \$150M+ water treatment plant. However, none of the 130+ subdivisions are within the represented geographic service area that was submitted to and adopted by the State Engineer for Grand Forks Traill Water Users and East Central.

East Central is seeking money damages against the City of Grand Forks in excess of \$60M. East Central’s complaint also demands that “any and all water lines, mains, meters, tanks, pump stations, valves, and other facilities owned or later constructed by Grand Forks and used to serve the disputed territory (being the 130+ subdivisions)” be turned over to them without any payment to the City of Grand Forks.

Because N.D.C.C. §6-09.4-22(2), and the provision that an agreement without the state lending entity as a party renders the agreement “invalid and unenforceable,” was never interpreted, this issue was presented to the North Dakota Supreme Court.

The City of Grand Forks argued this provision of the statute may render the agreement voidable but not void from the beginning – thus, after 20+ years, it would lend itself to finding the 2000 Agreement is no longer subject to be avoided by East Central. East Central, on the other hand, argued this provision rendered the 2000 Agreement void, *ab initio*, or from the very beginning and in turn legally as if this agreement never existed.

The North Dakota Supreme Court issued its decision in July, 2024 concluding the language of “invalid and unenforceable” found in N.D.C.C. § 6-09.4-22(2) renders an agreement without the state lending entity as a party, void, *ab initio*, or from the beginning.

The legislation change by HB 1537 is being proposed to avoid the inequitable result that East Central seeks against the City of Grand Forks by avoiding honoring its promises and commitments made in the 2000 Agreement, and performed for 20+ years thereafter. Moreover, such inequitable result is not confined to simply the City of Grand Forks as it appears there are a number of other municipalities that have similar such long-term agreements which do not include the state lender as a party. Of particular significance is that it has been discovered the state lending agencies have never signed off on any such agreements. Rather, they rely upon their lending documents to address these situations.

Further, this legislation will not imperil any water system financially, when considering in the example of East Central, they continued to receive loans from state agencies without issue. It is important to note that the protections afforded by both the federal and state statutes have no application unless there is a qualifying loan from a federal or state lending agency. Without such a qualifying loan, the statutes and protections under these statutes have no application. Thus, the clear import of these statutes is to protect repayment security of these lending agency. Nothing in the amendments alters these repayment security protections afforded to the state lending agencies.

In addition, when one considers the cost share opportunities with the State Water Commission to rural water districts, the cost and expense for infrastructure development by rural water districts has been greatly reduced. Although it should be noted that under N.D.C.C. § 61-35-26.3, before a grant or loan can be provided by the State Water Commission for a “water service project in any area within the extraterritorial zoning jurisdiction of any affected city” the rural water district is required to have an agreement with the effected municipality. Thus, given East Central’s position that the 2000 Agreement was void from the beginning, it calls into question the status of cost-share grants the State Water Commission has provided to East Central over years.

In sum, the City of Grand Forks seeks this committee’s favorable review of HB 1537 because the legislation is simply directed at having entities that entered into these types of agreement honor their promises and commitments.

The City of Grand Forks asks for a DO PASS for HB 1537.