ADDENDUM MATERIAL

DATE 8-16-21 ITEM NO. ADD 11

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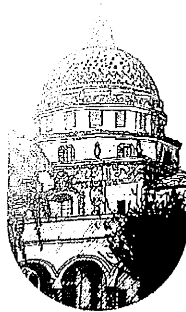
Pima County Attorney



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To: C.H. Huckelberry, County Administrator

From: Michael LeBlanc, Deputy County Attorney

Date: July 28, 2021

Subject: Legal Options Available to Challenge the Differential Water Rates Adopted by the City on June 22, 2021

On May 26, 2021, I provided you with a memorandum outlining the legal issues raised by the City's proposal to adopt differential water rates based solely on whether a customer receives service in unincorporated Pima County. In the memorandum, I explained that if the City adopts the differential rates, I would submit another memorandum addressing the specific causes of action, potential remedies, and the risks of litigation for the County and the unincorporated customers affected by the adopted rate structure. On June 22, 2021, the Mayor and Council (the "Council") unanimously adopted Ordinance 11846 which amends the Tucson Code to impose on unincorporated customers the differential water rate presented as Option 7 by Tucson Water. To the extent that Tucson Water provides service to customers within the incorporated areas of other cities and towns, the Ordinance doesn't apply to those customers. Therefore, I'm providing the following analysis as requested.

1. *The Adoption of City Ordinance 11846*

According to the City Clerk's Legal Action Report for the June 22 meeting, the Board adopted Ordinance 11846 with several conditions.[1] First, the Council approved the differential rates that Tucson Water presented as Option 7 which increases an unincorporated customer's base rate and fees by 10%.

[1] At the time of this memorandum, neither a copy of the approved minutes for the June 22 meeting nor the final version of Ordinance 11846 was available.

Option 7 also escalates the percentage of increase for higher usage tiers up to 40%. For your convenience, I've attached the rate sheet for Option 7 to this memorandum.

The second condition requires Tucson Water to spend the additional revenues generated by the differential rates on three programs:

1) Infrastructure maintenance and upgrades to enhance water delivery from the City limits to outside City limits,
2) Climate Resiliency and Water Sustainability for recharge, retention and reclamation projects (primarily outside the City limits) and enhancing the tree canopy throughout the entire Tucson water system, and
3) Financial resiliency in the form of expansion of the low-income program and a one time pay down of eligible delinquent accounts that have been negatively impacted by COVID-19.

The third condition sets December 1, 2021 as the effective date of the Ordinance. Before the effective date, Tucson Water must complete a cost of service analysis based on Option 7 that considers the economic and environmental benefit to the region. However, in adopting the Ordinance, the Council determined that Option 7 "results in reasonable differential water rates and advances critical policy considerations." It's unclear how the Council made this determination without the benefit of the analysis that it directed Tucson Water to complete.

2. *Additional Issues Raised by the Adoption of the Ordinance*

While the issues that I outlined in my May 26 memorandum remain unresolved by the Council's adoption of the Ordinance, the adoption raised additional issues that would be pertinent to the County's legal strategy.

a. *The spending of revenues generated by the differential rates on low-income and delinquent accounts is arguably illegal.*

A.R.S. § 9-511.01(G) provides that "[f]or residential property of four or fewer units, a municipality shall not require payment of unpaid water and wastewater service rates and charges by anyone other than the person who the municipality has contracted with to provide the service, who physically resides or resided at the property and who receives or received the service." The Legislature added this prohibition to the statute in 2010 and it mirrors the same prohibition for public utilities in A.R.S. § 40-376. One sponsor of the bill, Senator Frank Antenori, explained that the purpose of the prohibition is to prevent municipal water utilities from charging new homeowners for the delinquent water bills of previous owners and from charging landlords for the delinquent water bills of the landlord's tenants.

But the Legislature's intent when it added the prohibition should not preclude a court from applying it to the City's spending of the differential rate revenue. When an Arizona court interprets a statute, it looks first to the plain language and, if the plain language is clear, the court applies it without looking beyond the language. The courts consider the plain language the "best and most reliable index of a statute's meaning." *City of Tucson v. Clear Channel Outdoor, Inc.*, 218 Ariz. 172, 178 ¶ 6 (App. 2008).

A court could apply the plain language of A.R.S. § 9-511.01(G) to determine that, to the extent the targeted low-income and delinquent accounts are for residential property of four or fewer units, the City is unlawfully requiring customers in unincorporated Pima County to pay for unpaid water and wastewater service rates and charges of other customers. Though this determination would not resolve the issue of whether the differential water rates are lawful, it would deny the City a primary policy objective for the Ordinance.

b. The Council's direction for Tucson Water to complete a cost of service analysis after adopting the differential rates in Option 7 underscores the irrationality and arbitrariness of the Ordinance.

On March 30, 2021, the Chair of the Citizen Water Advisory Committee ("CWAC") notified the Council that a majority of the CWAC members voted to oppose differential rates. One of the half-dozen reasons the majority cited for its vote was the fact that "[t]he proposed differential rates are not linked to cost of service." The members expressed their concern that "de-linking rates from cost of service, and thereby charging an arbitrary higher rate for those customers in unincorporated Pima County would not only be divisive but would establish a dangerous precedent."

The City Attorney's Office had similar concerns for adopting differential rates without a cost of service analysis. In his June 15, 2021 memorandum to the Interim Director of Tucson Water, Principal Assistant City Attorney Chris Avery recommended that any proposed differential rate be analyzed before final adoption because "[t]o the extent that the rates are entirely or 'to the extent possible' based on proportional costs of service, the rates would be reasonable under *Jung* and A.R.S. § 9-511.01, and would also be consistent with Tucson Code § 27-32."[2] He further recommended that the Council should "amend Tucson Code § 27-32 alongside any such rate or revenue increase to reflect that policy decision; to expressly hold that rates for customers within the unincorporated area will be set in proportion to costs, plus a reasonable differential."

Rather than take the advice of its counsel and the CWAC, the Council adopted the differential rates in Option 7 without an analysis of the costs of service to unincorporated customers and without amending Tucson Code § 27-32. Instead, the Council directed Tucson Water to do the analysis after the Council had already determined that Option 7 "results in reasonable differential water rates and advances critical policy considerations." But the analysis would not be necessary if the Council had a fair and reasonable basis for adopting the Ordinance.

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[2] Section 27-32 of the Tucson Code provides: "Charges for water utility service shall be made at monthly intervals and shall, to the extent possible, be consistent with the policy for charging for water in direct proportion to the cost of securing, developing and delivering water to the customers of the city water system. Water charges will be computed through the summation of service charge, the monthly water use charge, the Central Arizona Project surcharge, the conservation charge and summer surcharges where applicable."

3. *Potential causes of action that Pima County may bring as a plaintiff in a lawsuit against the City.*

The causes of action that the County may bring that will most likely succeed in a challenge to the Ordinance are claims for injunctive and declaratory relief. If the County decides to pursue a lawsuit, the County should consider hiring outside counsel.

a. *The County very likely has standing and the capacity to sue for its claims against the City.*

For the County to challenge the differential water rates in Arizona Superior Court, it must have standing and the legal capacity to bring the lawsuit.[3] Standing and the capacity to sue or be sued are related but distinct concepts. Capacity relates to a party's right to come into court and litigate issues regardless of the nature of the claim. Because the County is a political subdivision of the state and is limited to the powers granted to it by the Legislature, the County's capacity to sue and be sued is established by A.R.S. § 11-201(A)(1).

To have standing to bring a lawsuit in Arizona, a plaintiff must allege facts that show "a distinct and palpable injury" caused by the defendant. *Sears v. Hull*, 192 Ariz. 65, 69 ¶ 16 (1998). The County may establish standing to bring its claims against the City in large part by relying on the facts presented in your June 24, 2021 Memorandum to the Board. The memorandum identifies 119 County-owned water connections that will incur the higher differential rates and provides an estimate of the costs to the County.[4] These facts will very likely establish the County's standing.

b. *The County has a reasonable likelihood of success in enjoining the enforcement of the Ordinance if it can show that the differential rates are not just and reasonable.*

The County may file an action for preliminary and permanent injunctive relief to prevent the enforcement of the Ordinance. Both a permanent and preliminary injunction are necessary because a trial on the merits of the case may not be resolved before the effective date of the Ordinance in December. A preliminary injunction would enjoin the enforcement of the Ordinance while the case is pending. However, one strategy for litigation may be to consolidate the hearing on the preliminary injunction with a trial on the merits, as allowed under Rule 65, which would expedite resolution of the case.

A plaintiff seeking injunctive relief must show:

1) For a preliminary injunction, a likelihood of success on the merits.
2) There is real threat of irreparable injury that is not remediable by damages.
3) A balance of the hardships among the parties favors the plaintiff.

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[3] The Superior Court has jurisdiction over class action lawsuits. If the County brings a challenge to the Ordinance without a class action, the Superior Court has jurisdiction over the claims for injunctive and declaratory relief.

[4] Attachment A of your June 24th Memorandum identifies one account for the Pima County Regional Flood Control District. If the District joins the lawsuit, it also will very likely have the capacity and standing to sue. A.R.S. § 48-3603(C)(12) authorizes the District, acting through its board of directors, to sue and be sued.

4) Public policy favors the injunction.

However, if a plaintiff can show that the act sought to be enjoined has been declared unlawful or against the public interest, the court presumes the threat of irreparable injury and that the balance of hardship favors the plaintiff. *Arizona Pub. Integrity All. v. Fontes*, 250 Ariz. 58 ¶ 27 (2020). The County has a strong argument to ask the court to make this presumption with regards to the Ordinance because the Legislature has declared in A.R.S. § 9-511.01(E) that "every unjust or unreasonable rate or charge demanded or received by a municipality is prohibited and unlawful." And if the court determines that the differential rates are not just or reasonable, the court should find that public policy would be served by enjoining the City's unlawful action. Likewise, if the County seeks to also enjoin the spending of the differential water rate revenue on paying low-income and delinquent accounts, the customer could argue that, under A.R.S. § 9-511.01(G) the Legislature has determined that requiring these payments to be against the public interest.

In addition to disputing the merits of the injunction, there are two defenses that the City might foreseeably raise in opposition. First, the City may argue that A.R.S. § 12-1802 prohibits the court from granting an injunction "[t]o prevent enforcement of a public statute by officers of the law for the public benefit." A.R.S. § 12-1802(4). Arizona caselaw is clear that "public statute" includes municipal ordinances and the City may argue that the prohibition applies because the City acted legally and within its power to set differential rates.

However, Arizona courts have consistently held that A.R.S. § 12-1802 does not prohibit injunctive relief against public officials who exceed their statutory authority or arbitrarily or unreasonably exercise their discretion. As outlined in my previous memorandum, the County has a reasonable argument that by failing to follow the required procedures for adopting rates under A.R.S. § 9-511.01 and by imposing rates based solely on whether a customer is in unincorporated Pima County, the Council arbitrarily and unreasonably adopted differential rates. This is further supported by the fact the rates do not apply to Tucson Water customers in other incorporated areas of the County.

The City may also argue that the County must exhaust administrative remedies before pursuing action in court. Section 27-50(2) of the City Code establishes a procedure for a customer who objects to "the actions, policies, or decisions of the water department with regard to utility service billing." The customer must first informally appeal to the billing office by phone, email, mail, or in person. If the billing office does not resolve the dispute, the customer has the right to an administrative hearing before a hearing officer. If the hearing officer finds that the customer's dispute is valid, the hearing officer has the authority to "make the appropriate corrections to the customer's account." The hearing officer's determination is final and the Code does not allow for an appeal of the determination.

If the City raised this defense, it would likely fail. While an injunction is inappropriate when an administrative remedy exists, courts require that the administrative remedy provide full relief to the plaintiff and cannot be futile. The City's administrative process is limited to challenge the "actions, policies, or decisions" of Tucson Water and is not available to challenge the rates set in an ordinance adopted by the Council. Therefore, the administrative process would not provide the County with full relief and would likely be futile because it would not address the legality of the Ordinance.

c. *The County has a reasonable likelihood of securing a judgment that declares the City's differential rates unlawful if the County can show that the Council did not comply with the statute when it adopted the differential rates or that the rates are not just and reasonable.*

A lawsuit for a declaratory judgment requests that the court declare the rights and duties of the parties without the requirement of an actual violation of a right or a breach of duty. Specifically, A.R.S. § 12-1832 allows declaratory relief to determine the validity of an ordinance and legal rights under an ordinance. Although a declaratory judgment is not coercive, it may be supplemented by injunctive relief as allowed by A.R.S. § 12-1838.

To obtain a declaratory judgment there must be an actual controversy among the parties and the judgment must terminate the controversy. It is unlikely a challenge to the Ordinance would fail this prerequisite. There is a controversy among the City and its unincorporated customers on whether the differential rates are lawful. The County could potentially raise two alternative claims for declaratory relief. First, the County may claim the Ordinance is unlawful because the Council failed to follow the procedures for providing the public with notice and the supporting report and data for the proposed differential rate under A.R.S. § 9-511.01(A)(1)&(2). Second, the County may claim the Ordinance is unlawful because the rates are not just and reasonable as required by A.R.S. § 9-511.01(E). Also, the County may consider requesting a declaration that the Council's direction to spend the revenue from differential water rates on low-income and delinquent accounts is unlawful under A.R.S. § 9-511.01(G). Declaratory relief is appropriate because by ruling on these issues, the court would resolve the controversy between the City and the County.

The procedure for obtaining a declaratory judgment does not differ from the procedure for obtaining any other form of judgment under the Rules of Civil Procedure. For example, the court could resolve the case on a motion to dismiss, a motion for summary judgment, or trial. At a trial the County would likely have the burden of proving the unlawfulness of the Ordinance by a preponderance of the evidence. It is unlikely the City would be entitled to a jury trial though it is a question for the court to determine whether that right exists.

d. *A court must award all costs and reasonable attorney fees to the successful party.*

A risk of litigation is, if the County is not successful in its challenge to the Ordinance, the court must award the City all of its costs in litigation, as allowed under A.R.S § 12-341, and the City's reasonable attorney fees, as allowed under A.R.S. § 12-348.01. *City of Tempe v. State*, 237 Ariz. 360, 367 ¶ 25 (App. 2015). On the other hand, if the County is successful in its challenge, it must be awarded its costs and reasonable attorney fees. The court uses the prevailing market rate as the basis to determine whether attorney fees are reasonable.

4. *Lawsuits brought by unincorporated customers other than Pima County.*
    a. *In addition to the claims that may be brought by the County, unincorporated customers may also bring a claim for injunctive and declaratory relief on the basis that the Ordinance is a violation of equal protection under the Arizona Constitution.*

In my previous memorandum, I explained that unincorporated customers have a good argument that the Ordinance violates equal protection. A customer could raise this argument to support a request for injunctive relief and as a basis for a declaratory judgment that the Ordinance is unlawful. A claim based on a violation of equal protection is not available to the County. Arizona courts have held that counties are not entitled to challenge a statute on equal protection grounds for the reason that a county is neither a citizen under the Arizona Constitution nor a person under the United States Constitution. *Trust v. County of Yuma*, 205 Ariz. 272, 277 ¶ 27 (App. 2003).

b. *If the County decides to join a large group of unincorporated customers challenging the Ordinance, the lawsuit will likely satisfy the requirements to certify a class action lawsuit under Rule 23 of the Arizona Rules of Civil Procedure.*

Rule 23 of the Arizona Rules of Civil Procedure allows a trial court to authorize a class action lawsuit and designate a single person or a small group of people to represent the interests of a larger group. Class action lawsuits serve as a practical tool for resolving multiple claims on a consistent basis at the least cost and with the least disruption to the judicial system. *Andrew S. Arena, Inc. v. Superior Ct. In & For Cty. of Maricopa*, 163 Ariz. 423, 425 (1990). In a 1990 opinion, the Arizona Supreme Court found "nothing… to suggest that the legislature intended to exempt public entities from either the burdens or the benefits of class actions in appropriate cases." *Id.*

There are three types of cases the court may certify as a class action. A lawsuit brought by a representative of unincorporated customers would likely qualify as two of the cases. Rule 23(b)(2) allows a class action where "the party opposing the class has acted or refused to act on grounds generally applicable to the class, so that final injunctive relief or corresponding declaratory relief is appropriate for the class as a whole." A lawsuit against the City would likely qualify because the City, through its Council, has acted to apply differential rates against unincorporated customers only. Injunctive and declaratory relief would be appropriate causes of action to challenge the Ordinance before it takes effect in December.

Rule 23(b)(3) also allows a class action where "questions of law or fact common to the class predominate over questions that affect only individual members and, [where] a class action is superior to other available methods for fairly and efficiently adjudicating the controversy." Given that the Ordinance applies Option 7 uniformly to all unincorporated customers, it seems unlikely that members of the class would raise individual questions that would predominate the questions common to the class, such as whether the differential rate is just and reasonable and whether the City has violated the unincorporated customers' right to equal protection under the law. A class action would arguably be the fair and efficient means to resolve these questions than many separate lawsuits brought by individual, unincorporated customers.

Rule 23 also requires that every class action satisfy four prerequisites:

1) The class must be so numerous that joinder of all members is impracticable. There is no fixed number for this requirement, "generally less than twenty-one is inadequate, and more than forty adequate, with numbers between varying according to other factors." *Ferrara v. 21st Century N. Am. Ins. Co.*, 245 Ariz. 377, 380 ¶ 8 (App. 2018).
2) There must be questions of law or fact that are common to the class.
3) The claims or defenses of the representative parties are typical of the claims or defenses of the class. Courts will merge this prerequisite with the second prerequisite for commonality because "both serve as guideposts for determining whether under the particular circumstances maintenance of a class action is economical and whether the named plaintiff's claim and the class claims are so interrelated that the interests of the class members will be fairly and adequately protected in their absence." *Id.* at ¶ 9.
4) The representative parties will fairly and adequately protect the interests of the class. In a challenge to the Ordinance, the plaintiffs representing the class should be current rate payers who are represented by counsel with experience in class action lawsuits. There should be more than one representative in case the court determines that one of the representatives cannot adequately represent the class.

The class representative seeking certification of the class has the burden of showing that the prerequisites are satisfied. The court has broad discretion whether to certify the class but considers only whether the requirements of Rule 23 are satisfied and not the merits of the plaintiffs' claims. After the court certifies a class action, the court must appoint class counsel based on factors set in Rule 23, though the court will likely appoint counsel selected and retained by the class representative. The Rule also sets specific requirements for proceeding with litigation including how to provide notice to class members and how to proceed with the settlement, dismissal, or compromise of the lawsuit. The court "may award reasonable attorney's fees and nontaxable costs that are authorized by law." Ariz. R. Civ. P. 23(h).

If the County pursues a class action against the City, the County should decline to represent the class. There is a potential risk that a court will not certify the class because there is no statutory authority for the County to sue as a representative in a class action lawsuit. Arizona courts recognize that a class representative has two separate claims in a lawsuit – the representative's own claim against the defendant and the claim that the representative is entitled to represent the class. *Douglas v. Governing Bd. of Window Rock Consol. Sch. Dist. No. 8,* 221 Ariz. 104, 109 ¶ 11 (App. 2009). While the County has clear authority to sue on its own behalf, I have not found any Arizona caselaw addressing whether a county's authority to sue under A.R.S. § 11-201(A)(1) necessarily implies an authority to represent the claims of a class.

There is also a potential responsibility for the County to pay costs and attorney fees for class representation if the County chooses to represent the class. The County may avoid the burden of paying all of these costs and fees if it agrees to a private plaintiff's attorney to represent the class. However, if the County decides to represent the class, our office is available to assist the County with identifying qualified counsel.

5. Conclusion

If the County seeks to challenge the Ordinance, it has the standing and capacity to sue the City. The County may sue on its own behalf or it may join a class of unincorporated customers in a class action lawsuit. The County, or the class of unincorporated customers, has a reasonable likelihood of success of bringing a cause of action to enjoin the enforcement of the ordinance and obtaining a declaration that the ordinance is unlawful based on claims that the Council did not follow the statutory procedures and that the differential rates are not just and reasonable. An unincorporated customer may also have a successful argument that the rates violate the equal protection clause of the Arizona Constitution.