

IN THE STATE OF SOUTH CAROLINA
In the Supreme Court

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APPEAL FROM RICHLAND COUNTY
Court of Common Pleas
The Honorable G. Thomas Cooper
The Honorable J. Ernest Kinard

S.C. Supreme Court

Docket No. 2011-CP-40-6705
Appellate Case No. 2014-000032

Joseph S. Azar, Frank J. Cumberland, Jr., and
Michael A. Letts, individually and as Class Representatives,

Appellants,

v.

City of Columbia,

Respondent.

**AMICUS CURIAE BRIEF OF
MUNICIPAL ASSOCIATION OF SOUTH CAROLINA**

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STATEMENT OF ISSUES ON APPEAL

The Municipal Association of South Carolina (“the Municipal Association”) adopts, as the issues on appeal, the Statement of Issues on Appeal presented by Respondent City of Columbia in its Final Brief.

STATEMENT OF THE INTERESTS OF THE AMICUS

The Municipal Association is a nonpartisan, non-profit association of the State of South Carolina’s incorporated cities and towns with 270 member municipalities. The Municipal Association, in addition to offering services and programs to its member municipalities, promotes and represents the collective interests of municipalities throughout the State. Municipalities have State Constitutional authority (Article VIII, Section 16) to construct or acquire and to operate public utility systems, including water, sewer, gas, electric, and transportation utilities. South Carolina has approximately 190 municipal water utility systems and approximately 100 municipal wastewater (sewer) utility systems. Municipal utility systems serve a substantial portion of the people, businesses and institutions of the State, both inside and outside of municipalities, and are a significant economic engine for our State.

Municipalities have a substantial and vital interest in judicial and legislative determinations of municipal rights and responsibilities concerning public utility systems. This Court’s September 9, 2015, decision would have a potentially adverse impact on the members of the Municipal Association who now own or operate, or may wish to own or operate, municipal public utilities. The Municipal Association believes that this Court’s decision rested on forced and inappropriate interpretations of S.C. Code § 6-1-330 and the Revenue Bond Act for Utilities (S.C. Code §§ 6-21-5 through 570) that are not supported by traditional principles of statutory interpretation and that are not supported by specific State statutes and established State case law.

The Municipal Association urges that this Court grant Respondent's Petition for Rehearing, rehear, reconsider and withdraw its decision of September 9, 2015, and issue a subsequent substituted decision affirming the judgment of the Circuit Court.

STATEMENT OF THE CASE

The Municipal Association adopts the Statement of the Case in the Final Brief of Respondent.

ARGUMENTS

I. THIS COURT'S DECISION MISCONSTRUES S.C. CODE § 6-1-330(B) AS APPLICABLE TO RATES AND REVENUES OF MUNICIPAL UTILITIES, AND THAT DECISION SHOULD BE REHEARD AND RECONSIDERED.

A. The Court's interpretation of S.C. Code § 6-1-330(B) fails to consider the import of the Constitutional authority of municipalities to operate public utilities.

Article VIII ("Local Government"), Section 16 ("Acquisition and operation of public utility systems") of the South Carolina Constitution provides, in pertinent part, that:

Any incorporated municipality may . . . acquire by initial construction or purchase and may operate gas, water, sewer, electric, transportation or other public utility systems and plants.

Prior decisions of this Court recognize this Constitutional grant of authority to municipalities as a limitation on the power of the General Assembly and as is the well-settled law of this State, "Constitutions are not grants of power to the General Assembly but are restrictions upon what would otherwise be plenary power." See Knight v. Salisbury, 262 S.C. 565, 206 S.E.2d 875, 876 (1974). This Court, in Green v. City of Rock Hill, 149 S.C. 234, 147 S.E. 346, 354 (1929), recognized that the right given by this section of the State Constitution (then Article 8, Section 5 of the Constitution of 1895) could not be withheld or withdrawn by the Legislature. This proposition of law was cited in Sossamon v. Greater Gaffney Metropolitan Utilities Area, 236 S.C. 173, 181, 113 S.E.2d 534, 538 (1960). The State Court of Appeals, in Calcaterra v. City of

Columbia, 315 S.C. 196, 197, 432 S.E.2d 498, 499 (Ct. App. 1993), explained that this Constitutional right of municipalities to operate public utilities “may be further implemented by legislation, but it may not be withdrawn or limited.”

The General Assembly, for this reason alone, could not have intended for section 6-1-330(B) to limit municipal authority to operate public utilities by (1) restricting the basis for utility rates to recovery of related costs of production or (2) removing the well-established right of municipal public utilities to operate for a profit and with a return on investment. This Court, in the absence of any express statement to the contrary in § 6-1-330, should not assume that the legislature intended to do what it is constitutionally prohibited from doing.

B. This Court’s decision failed to consider other earlier and more specific statutes dealing with municipal utility rate considerations that should prevail over the general “service and user fee” statute of § 6-1-330.

As recognized in another context in this Court’s decision in this case, “[t]he general rule of statutory construction is that a specific statute prevails over a more general one.” In keeping with its authorization under Article IX, § 1 of the State Constitution to “provide for appropriate regulation of . . . publicly owned utilities and privately owned utilities serving the public as and to the extent required by the public interest”, the General Assembly enacted a number of specific statutes dealing with municipal water and sewer systems, prior to the enactment of the general statute § 6-1-330 in 1997. *See, generally*, as related to rates and nonresident service, S.C. Code § 5-7-60 (“Municipality authorized to perform any of its functions or to furnish any of its services; charges and financing”), § 5-31-610 (“Construction and operation of municipal utilities”), § 5-31-670 (“Furnishing water for compensation; sewerage charge”), § 5-31-890 (“Contracts as to systems of sewage disposal”), § 5-31-1910 (“Authorization for cities and towns to furnish water and electric current beyond corporate limits”), and § 6-15-60 (“Sewer charges authorized”).

None of these specific statutes require that utility system revenues only be used to pay costs related to the provision of utility services.

Additionally, specific statutes address rates and revenues for water (and electric utilities) provided by commissions of public works for certain cities and towns. *See, generally*, S.C. Code § 5-31-210 *et seq.* A Commission of Public Works (“CPW”) sets rates independently of the municipal council. Because of this, a CPW does not appear to fall under the definition of a “local governing body” in § 6-1-300 (3). Under this Court’s decision, this would appear to mean that, while utility rates set by a municipal council are subject to § 6-1-330(B), utility rates set by a CPW would not be subject to the revenue restriction of § 6-1-330(B). This inconsistent treatment is another reason § 6-1-330(B) should not be read to include utility rates and is another apparent unintended consequence of this Court’s decision.

Prior to the passage of Act No. 138 of 1997 (part of which is now codified as S.C. Code § 6-1-330), this Court had provided over a century of guidance on the charges that could be imposed for water and sewer service and the uses that could be made of the revenues of such charges. In general, this Court endorsed the theory that a municipal utility system (whether it be water, sewer, electricity, natural gas, or some combination thereof) is an income-producing asset that is owned by the residents of the municipality. *See, generally*, Doyle v. Rosen, 229 S.C. 67, 91 S.E.2d 887 (1956) (providing for the combination of utility services); Simons v. City Council of Charleston, 181 S.C. 353, 187 S.E. 545, 546 (1936) (Stating with respect to the utility system as a business enterprise of the city that “it is incumbent upon a municipal corporation to exercise its judgment in a manner that will inure the greatest benefit of the city and its inhabitants.”); and Sossamon v. Greater Gaffney Metropolitan Utilities Area, 236 S.C. 173, 113 S.E.2d 534, 538 (*Referencing Green*, 149 S.C. 234, 147 S.E. 346, 356 for the proposition that “a city waterworks

system has been characterized as of a commercial nature.”). Income produced by the utility system asset may lawfully be used, indeed *should* be used, by the municipality to reduce the tax burden on its residents. In keeping therewith, municipalities have provided and continue to provide many services that are essential for the growth of an area densely populated enough to sustain a utility system – services like police protection, fire response, roads, bridges, and sanitation – through the imposition of taxes. And in many cases, taxes funded the initial construction of the utility system before revenues were sufficient for the system to become self-sufficient. In turn, the taxpayers of the municipality were entitled to a return on investment from the utility system that they helped to create. On this basis, usage of utility revenues for general governmental purposes does not render the enterprise revenue fund a “slush fund,” (*see Azar v. City of Columbia*) but rather constitutes a municipality’s informed decision as to the most beneficial use of its utility enterprise, that of promoting and supporting the city at large. 2015 S.C. LEXIS 325 (S.C. Sept. 9, 2015)

For example, in *Childs v. City of Columbia*, 87 S.C. 566, 70 S.E.2d 296, 297 (1911), the plaintiff non-resident of the City argued that the City lacked the right to charge “exorbitant, discriminatory and unreasonable” rates to its nonresident customers. The Court disagreed, reasoning that:

... the duty to sell the excess of its water supply did not import an obligation to make a contract with any particular person at a reasonable price, but on the contrary did import an obligation to sell its surplus water for the sole benefit of the city at the highest price obtainable: it was a duty not owed to outsiders, *but exclusively to inhabitants and taxpayers of the city.*

70 S.E.2d at 298 (emphasis added). The duty owed to the “inhabitants and taxpayers of the city” is clearly to maximize the revenues reasonably generated by the utility system in order to lessen the burden on such taxpayers. *See Simons*, 181 S.C. 353, 187 S.E. 545, 546 (1936) (Providing

that authorizing the use of revenues to pay bonds “will be a relief to its general taxpayers.”), and Sloan v. City of Conway, 347 S.C. 324, 331, 555 S.E.2d 684, 687 n. 10 (2001) (“Raising revenue to meet increasing municipal needs is a legitimate governmental goal and selling water at higher rates to customers who do not pay taxes is rationally related to that goal.”).

The enactment of § 6-1-330 does not affect the considerable legal precedent applicable to utility charges. In fact, § 6-1-330 was enacted specifically to respond to a case in which this Court held that municipalities and counties could enact local hospitality and accommodations fees under their home rule powers. *See* S.C. Code § 5-7-30; *also see* Hospitality Association of South Carolina, Inc. v. County of Charleston, 320 S.C. 219, 464 S.E.2d 113 (1995). The South Carolina General Assembly responded by passing Act No. 138 of 1997, which provided specific statutory guidance for local option sales taxes, accommodations taxes, and hospitality taxes. In addition, Act No. 138 provided general guidelines for the imposition of a “*new* service or user fee.” S.C. Code § 6-1-330 (emphasis added); *also see* S.C. Code § 5-7-30 (authorizing the implementation of uniform service charges or charges for services previously paid from the proceeds of *ad valorem* property taxes). Of course, municipalities *already* had the power to impose charges for the sale of water and sewer service, both under their home rule powers and under S.C. Code § 5-31-670 (municipalities may “furnish water to persons for reasonable compensation and charge a minimum and reasonable sewerage charge for maintenance or construction of such sewerage system”).

- C. This Court’s decision overlooks clear language of § 6-1-330 limiting its applicability to “new” fees.

The second sentence of § 6-1-330 (A) refers to “new” service or user fees. The fourth sentence of § 6-1-330 (A) explicitly states:

A fee adopted or imposed by a local governing body prior to December 31, 1996, remains in force and effect until repealed by the enacting local governing body, notwithstanding the provisions of this section.

This Court failed to consider the explicit “prospective only” application arising from this language, as well as the implied “prospective only” application arising from § 6-1-330’s effective date of July 1, 1997, as discussed in the order of the circuit court.

To read the revenue restrictions of § 6-1-330 as retroactively impairing the ability of municipalities to operate their utilities would, in effect, be an implied repeal of the pre-existing statutory and judicial guidance on municipal water and sewer rate setting. A later enacted general statute does not repeal an earlier more specific statute. Spartanburg County Department of Social Services v. Little, 309 S.C. 122, 420 S.E.2d 499 (1992). Furthermore, repeal by implication is not favored and will be applied only when two statutes are incapable of any reasonable reconciliation. City of Rock Hill v. S.C.D.H.E.C., 302 S.C. 161, 394 S.E.2d 327 (1990).

In short, S.C. Code § 6-1-330 does not apply to utility charges. Therefore, this Court erred in applying the “related to” standard of § 6-1-330 to such charges. Of course, there *are* limits on the disposition of utility revenues and standards for maintenance and operation of utility systems, and correcting this Court’s misreading of § 6-1-330 would not leave municipal utility systems completely unregulated. For example, rating agencies and financial institutions routinely examine the transfer policies of municipalities and penalize municipalities that are overly dependent on expenditures and transfers from their enterprise funds – as is appropriate given their commercial nature. In particular, the major ratings agencies, i.e. Standard & Poor’s and Moody’s Investors Service, specifically acknowledge that their rating methodologies examine and consider a public utility’s general fund transfer policy as a significantly weighted factor in determining such utility’s underlying credit quality. In addition, regulatory agencies

(State and Federal) and permitting requirements ensure that a municipal utility system will remain compliant with standards that protect the health, safety, and welfare of the general public.

- D. This Court's decision incorrectly fails to distinguish between charges for governmental "services and programs" and charges for essentially commercial transactions, and therefore erroneously concludes that S.C. Code § 6-1-330 applies to utility charges.

In its decision, this Court states that "[t]he City admits the monies at issue fall within the definition of 'service or user fee' as the term is statutorily defined." Azar, 2015 S.C. LEXIS 325 at *5. The Municipal Association and its member municipalities, however, do not admit that utility charges are subject to S.C. Code § 6-1-330, strongly disagree with such application and would vigorously contest that conclusion in future cases. Therefore, this Court's substantive discussion of the applicability of S.C. Code § 6-1-330 should be reconsidered and removed from the decision.

In a footnote, this Court dismisses the argument that, in providing water and sewer to customers, a municipality is acting in a "proprietary capacity." This Court argues that "'proprietary capacity' is essentially an accounting concept [and that,] [w]ith no supporting authority, the City vastly overestimates the significance of its purported 'proprietary capacity.'" Azar, 2015 S.C. LEXIS 325 at *7-8 fn. 4. Accounting concepts do contain the term "proprietary capacity," but this Court has also repeatedly used that term or its equivalent to make distinctions that go well beyond mere accounting treatment. *See* Sossamon v. Greater Gaffney Metropolitan Utilities Area, 236 S.C. 173, 113 S.E.2d 534 (1960); *see also* City of Beaufort v. Beaufort-Jasper County Water & Sewer Auth., 325 S.C. 174, 480 S.E.2d 728 (1997); *see also* BellSouth Telecommunications, Inc., v. City of Orangeburg, 337 S.C. 35, 522 S.E.2d 804 (1999). The South Carolina cases are not entirely consistent on the meaning of "proprietary capacity," but

this Court has consistently recognized that certain activities of municipalities are “proprietary”, essentially meaning commercial or business-like.

For example, in Sossamon, 236 S.C. 173, 113 S.E.2d 534 (1960), this Court invalidated an Act of the General Assembly that forced the City of Gaffney to provide water service to customers outside of its territorial boundaries. As described by this Court, “[t]he Act imposes upon the City of Gaffney the duty of furnishing water to those outside its corporate limits. Other municipalities may choose not to do so.” Sossamon, 113 S.E.2d at 538. Moreover, reasoned the Court, “[t]his obligation placed upon the city must be discharged without profit. All other municipalities are at liberty to charge ‘reasonable compensation’ and make a profit on utility service outside their corporate limits.” Id. In considering the Act, the Court noted that “there can be no doubt that in the fiscal aspect thereof the operation and maintenance of such utility partake largely of the nature of a commercial or business enterprise.” Id. (emphasis added). Given that the City of Gaffney had the constitutional right to own and operate its water system, and to do so in a “commercial or business capacity,” the Court found that “the Legislature may not without [the City’s] consent and without compensation appropriate in whole or in part such water system to the use of the inhabitants of another governmental unit.” Id. at 539.

The Court has also insisted that, in contractual matters, the distinction between governmental and proprietary functions remains crucial. In a case challenging the validity of a contract that purported to give certain municipalities a first right of refusal to provide extra-territorial utility service, the respondent argued that the State of South Carolina made no distinction between governmental and proprietary functions of municipalities. See City of Beaufort, 325 S.C. 174, 480 S.E.2d 728 (1997). The Court rejected this argument, explaining that “[t]his language is limited to actions brought in tort because case law is clear that in determining

the validity of municipal contracts, the distinction between governmental and proprietary functions is significant, if not dispositive.” City of Beaufort, 325 S.C. at 179 n.3, 480 S.E.2d at 731 n.3.

The Court has previously explained, in language directly applicable to this case, the significance of concluding that a municipality is acting in a proprietary capacity. In a case considering a challenge to a municipal franchise fee, the Court made clear that the analysis contained in Brown v. Horry County, 308 S.C. 180, 417 S.E.2d 565 (1992), did not apply. See BellSouth Telecommunications, Inc., 337 S.C. 35, 522 S.E.2d 804 (1999). The plaintiff had argued that the franchise fee was in fact a tax under Brown because the proceeds were deposited into the municipality’s general fund.

Where a municipality seeks to justify a charge as a fee because the revenue generated by the charge is used for the payer's benefit, we will consider the fact that the revenue is placed in a municipality's general fund in deciding whether or not the payer specially benefits from imposition of the charge. This factor is irrelevant, however, where the benefit to the payer derives not from the municipality's use of the revenue but is a benefit given directly and solely to the payor in exchange for the fee. In exchange for the fees imposed in this case, BellSouth is granted the special privilege of using public streets to place its equipment in order to serve City's residents and generate private profit. The fact that the fees are placed in City's general fund is irrelevant.

BellSouth, 337 S.C. at 40, 522 S.E.2d at 806 (emphasis added). In other words, when a municipality acts in a “proprietary capacity” by entering into an essentially commercial transaction, the amount paid by the purchaser is neither a tax nor a service or user fee under Brown. For example, a municipality may dispose of obsolete vehicles or equipment by selling them to private parties. The revenues of that transaction are neither a tax nor a fee. Likewise, a municipality may sell tickets to a performance at a publicly-owned venue; again, the revenues are not taxes or fees. In the case of water and sewer service, the customer enters into a conceptually identical transaction. In exchange for the payment of a mathematically calculated

“price,” set by a rate schedule, the customer receives a definite amount of water or discharges a definite amount of waste. On the other hand, all of the cases following Brown have involved general government programs or services that cannot be reduced to a simple purchase and sale arrangement. Given that S.C. Code § 6-1-330 is essentially a codification of the Brown analysis, BellSouth demonstrates the inapplicability of that statute to utility charges as well.

As clearly explained by the Court in BellSouth, the plain language of the “service or user fee” statutes does not attach to utility revenues. Under S.C. Code § 6-1-300(6), the restrictions of § 6-1-330 apply to “charge[s] required to be paid in return for a particular government service or program made available to the payer” (emphasis added). Utility charges are not imposed for a service or program, but for a commodity or a private good. The person who pays a water or sewer charge is buying water or paying for the disposal of wastewater. The benefit of that transaction is immediate and particular; such person is entering into a commercial transaction with the government to purchase a particular thing.

- E. This Court’s decision fails to consider that § 6-1-330 has no express extra-territorial application and does not apply to charges of nonresident utility service contracts.

For more than 100 years, this Court has recognized the legal principle that:

All powers and privileges conferred by the Constitution and statutes on municipal corporations must be held to be limited in their exercise to the territory embraced in the municipal boundaries and for the benefit of the inhabitants of the municipality, unless the Constitution or statute expressly provides that such powers and privileges may be exercised beyond the corporate boundaries, or for the benefit of nonresidents.

Childs v. City of Columbia, 87 S.C. 566, 70 S.E. 296, 298 (1911). Section 6-1-330 contains no express provision that it is applicable to any “service or user fee” imposed for municipal services

beyond the municipal boundaries or for nonresidents. Yet, this Court's decision, contrary to Childs, reads extra-territorial application into the statute.

It is clear, under our State's statutory and case law, that municipal utility services, including water and sewer, are provided to areas outside of the corporate limits by contract with service charges set by contract. *See* S.C. Code § 5-7-60, S.C. Code § 6-31-1370, S.C. Code § 6-31-1520, S.C. Code § 6-31-1910, and Childs, 87 S.C. 566, 70 S.E. 296, 298 (1911), Calcaterra, 315 S.C. 196, 197, 432 S.E.2d 498 (Ct. App. 1993) and Sloan, 347 S.C. 324, 555 S.E.2d 684 (2001). In Sloan, this Court, among other things, viewed Childs as holding that a provision as to municipal water service, "whether constitutional or statutory, does not apply for the benefit of nonresidents unless expressly provided." 347 S.C. 324, 330, 555 S.E.2d 684, 687. This Court's decision overlooked this requirement of our case law and failed to consider that § 6-1-330(B) does not expressly apply to revenues from nonresidents.

II. THIS COURT'S DECISION MISINTERPRETS THE REVENUE BOND ACT FOR UTILITIES, CODIFIED AT S.C. CODE §§ 6-21-5 THROUGH 570.

The Revenue Bond Act for Utilities ("the Revenue Bond Act") authorizes the issuance of bonds for the purchase or construction of designated public works, and provides the terms upon which the borrower may contract with the bondholders for the operation and maintenance of the public works and the disposition of the revenues thereof. The Court fundamentally misunderstands the purpose of the Revenue Bond Act in protecting the rights of bondholders and erroneously concludes that the Revenue Bond Act sets forth independent, substantive standards that govern a municipality's disposition of water and sewer revenues irrespective of its contract with the bondholders. The Court's error creates an unworkable, burdensome, and illogical environment in which municipalities will be subject to costly and intrusive litigation based on the structure of its borrowings. More specifically, the Court errs in (a) concluding that the

contractual rights that exist for the protection of bondholders under the Revenue Bond Act create independent, third-party rights that can be enforced by any interested party; (b) failing to differentiate among municipalities that have issued bonds under the Revenue Bond Act, that have issued bonds under the Revenue Bond Refinancing Act of 1937 (or both statutory schemes), or that have not issued bonds at all; and (c) allowing private litigants to demand judicial review of complex, interrelated, and long-term capital planning decisions made by elected officials.

- A. The provisions of the Revenue Bond Act relating to disposition of revenues serve to protect the rights of, and are enforceable only by, holders of bonds issued thereunder.

This Court cites S.C. Code § 6-21-440 for the proposition that “[i]t is only after the utility system's operating and maintenance expenses and bond principal and interest expenses have been paid and the statutorily required set-asides have been made in the depreciation and contingent funds that ‘[a]ny surplus revenues thereafter remaining’ may be used for unrelated purposes at the local government's discretion.” Azar, 2015 S.C. LEXIS 325, at *12 (emphasis added). The Court ignores the opening sentence of this section, however, which provides that the municipality shall establish the “separate and special funds” listed in the section “[i]n the authorizing ordinance” pursuant to which the bonds are issued. In other words, the municipality actually negotiates the provisions of the “required set-asides” with the prospective purchaser of the bonds, and the result of that negotiation is embodied in the authorizing ordinance. See City of Spartanburg v. Blalock, 223 S.C. 252, 261; 75 S.E.2d 361, 365 (1953) (the Court, in interpreting the provisions of the Revenue Bond Act, stated that the establishment of the distinct accounts under § 6-21-440 is for the protection of bondholders). This reading conforms to custom and

practice as some prospective bond purchasers will require definite set-asides and others will be more flexible.

By the terms of the City of Columbia's General Bond Ordinance dated May 21, 1993, as so amended and supplemented, the City has covenanted with its bondholders to fund its set-asides as follows: all revenues collected by the City from the operation of the utility system are deposited into the City's General Revenue Fund; thereafter, the revenues shall be used to make payments in the following order of priority: first, for the payment of operation and maintain expenses for the utility system; second, into the respective Debt Service Funds¹; third, into the respective Debt Service Reserve Funds², if any; and fourth, to the extent there are remaining revenues, such revenues shall be used to, first, pay debt on junior lien obligations, second, to provide funds to build a reserve for the utility system to pay for depreciation and other contingencies and, third, used by the by the city for such purposes as it may determine. *See, generally*, Ordinance 93-43 of the City of Columbia dated May 21, 1993, Article VI – "Establishment of Funds; Security For and Payment of the Bonds; Investment of Moneys."

Outside of maintaining "debt service coverage"³ of 110%, the City, like many other municipalities, has not covenanted with its bondholders under its Bond Ordinance and is therefore not required to fund depreciation or contingency costs at a set amount. As a result, the City, as a legislative body and in consideration of the current and future needs of its system and its taxpayers, may decide what amounts to fund toward depreciation and contingency costs or whether to fund such set-asides at all.

¹ Which fund is synonymous with the Bond and Interest Redemption Funds in S.C. Code § 6-21-440, and a new Debt Service Fund is established for every separate Bond issued by the City.

² This is a special fund that is funded on an issue-by-issue basis at the discretion of bondholders and typically is maintained in an amount equal to one-year in debt service on the bonds they secure, if any, as required by a bondholder.

³ Revenues of the utility fund, less operating expenses divided by the annual debt service coming due on the City's bonds.

Other municipalities may, however, be required by their bondholders to actually fund separate depreciation and contingency funds. The United States Department of Agriculture – Rural Development⁴, for example, frequently lends to smaller and more financially challenged municipalities. As a result, Rural Development typically requires that the depreciation fund and the contingent funds will each contain at least one year’s worth of debt service, and allows the borrower to build up that amount over time by monthly deposits.⁵

Even for larger municipalities, the bond market may exert pressure to maintain adequate amounts of reserves for depreciation and contingencies. A municipality that is rated by any of the major rating agencies will face questions about the adequacy of its depreciation and contingency funding, as will a municipality that seeks to directly place a bond with a financial institution. A perceived deficiency in depreciation and contingency funding might well cause higher interest rates, lower bond ratings, or even contractual covenants to increase the funding levels.

The point is that the bondholders have the right, as a condition of their contractual agreement to purchase the municipality’s bonds, to determine the appropriate amounts to be set-aside for depreciation and contingencies. The bondholders may, and often do, decline to impose a specific target for such amounts. In that event, the municipality determines for itself – subject to the review of the ratings agencies, the interest rates charged by lenders, and the regulatory requirements of regulatory bodies – the amounts that represent a “sum sufficient” for depreciation and contingencies.

This Court’s reading of the Revenue Bond Act, however, would take this contractual right to require set-aside funding *away from the bondholders*, and would turn it into a

⁴ The City of Columbia does not have any outstanding utility revenue bonds held by Rural Development.

⁵ Typically over ten years.

freestanding, independent right for any litigant⁶ to demand that a court review a municipality's capital planning, depreciation and contingency funding, and internal decisions on deferred maintenance and system improvements. In many cases this review might actually *harm* the interests of bondholders, as the municipality incurs costs in defending legal challenges to its capital planning, forgoes pay-as-you-go capital improvements in order to "save up" an arbitrary depreciation and contingency "sum-sufficient" that would satisfy any potential litigant, and otherwise ties up capital in possibly nonproductive uses.

This Court should therefore reconsider its decision to allow litigants and courts to interfere with the contractual relationship between a municipality and its bondholders. At a minimum, this Court should require that standing to bring a suit under the Revenue Bond Act requires that the litigant actually be a bondholder.

- B. The City of Columbia and other municipalities are authorized to borrow under statutory schemes other than the Revenue Bond Act, or may not borrow at all, and this capital planning decision should not determine a municipality's ability to apply and dispose of surplus revenues.

Section 14 of Article X of the South Carolina Constitution authorizes the issuance of indebtedness payable solely from a revenue producing project or from a special source, upon the conditions prescribed by the General Assembly and the legislature has authorized other statutory provisions regarding the issuance of bonds secured by a pledge of a municipality's utility revenues.

This Court considers only the Revenue Bond Act in concluding that surplus revenues may be disposed of only after the City has adequately funded depreciation and contingencies. However, the City is additionally authorized under the South Carolina Constitution and its Bond

⁶ It should be noted that under the City's Bond Ordinance dated May 21, 1993 that individual bondholders do not maintain a private right of action against the City in the event of a default; rather only bondholders maintaining a collective 25% of the Bonds outstanding may act to enforce the remedies under the Bond Ordinance and the Bonds.

Ordinance to borrow under the Revenue Bond Refinancing Act of 1937, codified at S.C. Code §§ 6-17-10 through 320 (“the Revenue Bond Refinancing Act”). The Revenue Bond Refinancing Act is clearly a statutorily authorized alternative for borrowing, and the City is authorized to issue utility revenue bonds under both statutes. While the Revenue Bond Act and the Revenue Bond Refinancing Act are substantially similar in that both statutes provide for the issuance of revenue bonds secured by a limited pledge of and lien upon a designated stream of revenues, there are fundamental differences between the statutes. The Revenue Bond Refinancing Act does not contain any provision comparable to § 6-21-440 of the Revenue Bond Act. When the City borrows under the Revenue Bond Refinancing Act, there is *no* requirement to establish depreciation or contingency funds and *no* explicit authorization to dispose of “surplus revenues.”

Likewise, a municipality simply might have no outstanding debt, either because it has never issued bonds or because it has repaid all of its prior bond issues. Would such a municipality be subject to the requirement to fund depreciation and contingency? If not, under what circumstances could it dispose of “surplus revenues?”

These questions reveal the Court’s misapprehension of the Revenue Bond Act and a municipality’s authorization to issue utility revenue bonds. Under this Court’s reading, the Revenue Bond Act both requires that the City fund depreciation and contingency and authorizes it to apply “surplus revenues.” The Court’s decision renders an otherwise straightforward statutory scheme uncertain - what happens if the City determined not to issue Bonds under the Revenue Bond Act? Would it mean that a municipality is not required to fund depreciation or contingency accounts and all revenues after paying operation and maintenance would be “surplus revenues?” Alternatively, does the Court’s holding mean that a municipality would not be subject to the requirement to fund depreciation or contingency, but that no revenues can be

transferred as “surplus?” This Court’s holding may cause the City (and all other municipalities affected by the Court’s decision) to stop using the Revenue Bond Act to issue bonds– or perhaps not to issue bonds at all – simply to secure the most flexibility with respect to its “surplus revenues.” Surely this would be an irrational outcome.

- C. Cities face complex, interrelated, and long-term decisions with respect to capital planning for their utility systems, and the court should not use the contractual provisions described in the revenue bond act to second-guess these decisions.

This Court’s decision instructs the lower court, on remand, to ask whether “the City has adequately funded the ongoing operating and maintenance expenses and satisfied the specific set-asides commanded by Section 6-21-440 of the Revenue Bond Act (including setting aside ‘sufficient’ sums in the depreciation fund and the contingent fund)” Azar, 2015 S.C. LEXIS 325, at *15. The stated standards (adequacy and sufficiency) are invitations to conduct unlimited inquiries into internal capital planning decisions that should not be subjected to the threat of unbounded judicial review.

For example, the interest rate market since at least the year 2000 has allowed municipalities to borrow at historically low rates. At the same time, this interest rate market has caused municipalities to earn next to nothing (and in some cases, actually nothing) on their reserve balances. In this context, sound capital planning suggests that it is more prudent to borrow to fund improvements *when* they are needed rather than to save to fund improvements *before* they are needed. Stated differently, it is financially imprudent in this interest rate environment for a municipality to be sitting on large reserves of cash for depreciation and contingency planning. This Court’s holding that a municipality *must* fund depreciation and contingency would distort such rational capital planning decisions.

Likewise, elected officials face complex questions on deferred maintenance issues. Under this Court's holding, a litigant could, in theory, compel a court to require that a municipality address its deferred maintenance needs before any revenues may be considered surplus. But, as is common with utility infrastructure, the municipality could plan to entirely replace aging infrastructure with new or different infrastructure or even to turn to other providers for service. For example, what if the municipality were planning to construct an entirely new treatment plant in five years⁷, or to decommission the existing treatment plant and pay an adjoining municipality for such services?⁸ In such a case, prudent capital planning would suggest that the municipality defer all but the most critical maintenance on the aging plant.

In short, complexities abound, and the question is not simple enough to reduce to "adequacy" of maintenance and "sufficiency" of reserves. A trial court could of course work through all of these issues, with appropriate expert testimony and detailed reviews of capital improvement plans and audits and budgets and, but the effort would be enormously costly for and invasive to the City and all similarly situated municipalities. Moreover, such a detailed review of decisions made by elected officials is almost paradigmatic of the areas that should *not* be subject to judicial second-guessing. In this light, the Court should reconsider its conclusion that the Revenue Bond Act creates an independent substantive standard for municipalities outside of their contractual relationships with their bondholders.

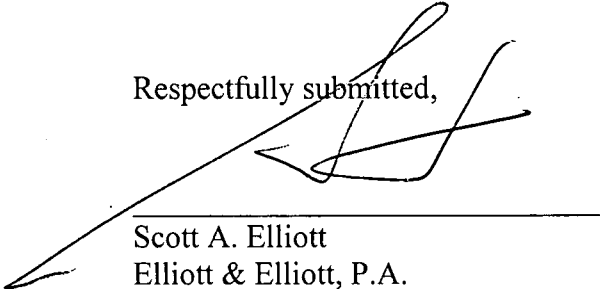
CONCLUSION

For the reasons stated above and in Respondent's Petition for Rehearing, this Court should rehear, reconsider and withdraw its decision of September 9, 2015, and affirm, in a substituted decision, the judgment of the Circuit Court.

⁷ For example, the City of Cayce recently built a new, regional wastewater treatment plant.

⁸ For example, the Cities of Hardeeville, Beaufort, and Port Royal all sold their public utility facilities to Beaufort-Jasper Water and Sewer Authority.

Respectfully submitted,

A handwritten signature in black ink, appearing to read 'S. Elliott', is written over a horizontal line. The signature is stylized and extends above and below the line.

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October 19, 2015

IN THE STATE OF SOUTH CAROLINA
In the Supreme Court

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OCT 19 2015

S.C. Supreme Court

APPEAL FROM RICHLAND COUNTY
Court of Common Pleas
The Honorable G. Thomas Cooper
The Honorable J. Ernest Kinard

Docket No. 2011-CP-40-6705
Appellate Case No. 2014-000032

Joseph S. Azar, Frank J. Cumberland, Jr., and
Michael A. Letts, individually and as Class Representatives,

Appellants,

v.

City of Columbia,

Respondent.

PROOF OF SERVICE

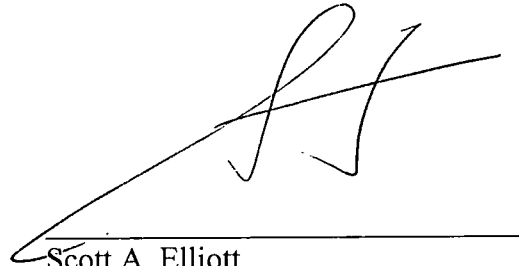
I certify that I have served the Amicus Curiae Brief of the Municipal Association of South Carolina on Appellants and Respondent by depositing a copy of it in the United States Mail, postage prepaid, on October 19, 2015, addressed as follows:

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October 19, 2015

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