

# Legally Relevant



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## What really happens when a city annexes land in a RWD? (Part II)

In the November 2006 *Lifeline*, we looked at what happens to the boundaries of a rural water district when part of its territory is annexed by a city. We found that the law is not as clear as some might think. The most likely answer is that rural water district territory annexed by a city is deleted from the territory of the district at the time the city actually provides for water service other than that formerly provided by the district.

That's all well and good, but what happens to the benefit units of the former rural water district customers whose land has been annexed? Those benefit units don't just vanish into thin air, do they? Is the customer entitled to any compensation for units owned? After all, courts have told us that benefit units are a form of property right, and the customers paid a good sum of money for them.

### What is a Benefit Unit?

To answer these questions, the starting point is to determine just what a benefit unit is. It is interesting that Kansas statutes don't provide a clear definition of the term "benefit unit." The statutes do tell us that the "total benefits" of rural water district "improvements" are to be divided into a suitable number of benefit units and that landowners are to subscribe to those units. Landowners' subscriptions are to be in proportion to the extent they wish to participate in the benefits of the improvements. The statutes also tell us that benefit units are to be issued on terms and conditions within the discretion of a rural water district's board of directors. Finally, the statutes tell us that when certain nonprofit corporations and cooperatives convert themselves to rural water districts, the members' shares of stock or membership certificates are converted to benefit units.

Having shares of stock or membership certificates converted to benefit units makes it sound like benefit units are some kind of ownership interest in a rural water district. But is that really the case? The answer there seems to clearly be "no"; rural water districts are units of government (quasi-municipal corporations, according to statute), and individuals don't own units of government.

Kansas statutes expressly provide for the enactment of bylaws by rural water districts. What do districts' bylaws typically say about the definition of benefit units?

As with Kansas statutes, most districts' bylaws don't expressly define what a benefit unit is. The language contained in such bylaws, however, gives us information from which we can

determine a definition. Most districts' bylaws state that a benefit unit entitles its owner to one line from a district's water system and that the line must serve only one residence or business.

District bylaws also typically provide that the district's board can adopt rules and regulations pertaining to the operation of the district. Keep in mind, too, that although Kansas statutes don't expressly define what a benefit unit is, they make it clear that a district's board of directors is to define the terms and conditions under which benefit units are to be issued. Putting these two things together, then, it seems logical to look to a district's rules and regulations to complete the picture concerning exactly what a benefit unit is.

Unlike Kansas statutes and districts' bylaws, districts' rules and regulations typically do provide a definition of the term "benefit unit." Such rules and regulations generally state that a benefit unit is a right to receive water service to meet a customer's requirements. Now things have become clearer. The statutory right to share in the benefits of improvements and the right from bylaws to one line from the district's water system, is the right to receive water service from the district.

### **Effect of the Annexation Statute**

The Kansas statute dealing with annexation of rural water district territory by cities is K.S.A. 12-527. Under that statute, a city annexing district land must negotiate with the district whose land is

being annexed in order to acquire title to facilities owned by the district within the annexed area. The city and the district may agree for the district to retain facilities used to transport water outside the city. If negotiations fail, three appraisers are to determine the fair market value of the "property,

facilities and improvements of the district annexed by the city," subject to review by the District Court on appeal.

So what happens if the negotiations between the city and the district are successful (or the negotiations are not, but the appraisers resolve the disputed value)? The statute states that the facilities

previously owned by the district become the property of the city upon payment by the city of the reasonable value of the facilities as determined by the parties. The city has the right, and as to those facilities not used to transport water through the annexed area to serve benefit units located outside the annexed area, the city has the duty to buy those facilities (unless, of course, the district and the city agree otherwise).

As was discussed in last issue's installment, the law appears to be that rural water district territory annexed by a city is deleted from the territory of the district at the time the city assumes responsibility for providing service or otherwise provides for service in the annexed territory. K.S.A. 12-527 clearly implies that when that occurs, the district no longer has the right to sell water service to the customers it previously served in the annexed area.



As was discussed above, a benefit unit is the right to receive water service from a rural water district. If, however, as a result of K.S.A. 12-527, a rural water district no longer has the authority to sell water service to a landowner, it follows that the landowner can no longer legally purchase water service from the district. When that happens, landowners who previously had benefit units no longer really have them, because they have no right to receive water service from a rural water district. Likewise, if the essence of a benefit unit is to have “one line” from the district’s water system, and the annexing city has just bought that part of the district’s system, it seems that the benefit unit has been extinguished. As a result, our firm has recommended that once the city assumes responsibility for providing service, the district’s board of directors adopt a resolution formally terminating the benefit units that were previously assigned to the land within the annexed area.

In such circumstances, landowners within that area are not left without service. They now have the right to receive water service from the annexing city that is providing service. So the landowners are still receiving what they paid for when they purchased their benefit units – that being the right to receive water service. It’s just that the water service being received comes from the city rather than the district.

Still, some sticky problems can arise. For example, what if some of the landowners in the annexed area also own land in other areas of the district – should they be permitted to transfer their units to their other land? Strictly speaking, the answer according to most by-laws may turn on whether the transfer is made before or after the annexation and assumption of service by the city (perhaps you can’t transfer a unit that has been extinguished).

### **Conclusion**

As with the discussion of the adjustment of territory in this column in the November 2005 Lifeline, it is not easy piecing together a reasonable explanation of what becomes of benefit units following annexation and assumption of water service by the city. The conclusions above are made easier by a couple of things. First, the Kansas Statutes on rural water

districts and annexation must be read together and all given effect if there is any logical way to do so, and those statutes lead to the conclusion that the annexing city will usually assume water service to the annexed area to the exclusion of the water district. Given this meaning, it is difficult to imagine how those benefit units can continue to exist under these circumstances. But, we are not aware of any court that has decided the matter. The day may come when a court gets that chance.

## **Legislative Update – Rural Water District Releases**

After the 2006 legislative session, featuring a considerable amount of dissatisfaction by some members of the Kansas Legislature with the law regarding releases of rural water district territory, a new bill has been introduced in the 2007 legislature. The bill, HB 2057, is the result of a study conducted by a committee organized by KRWA, including rural water district board members, managers and attorneys. The committee tried to reconcile landowners’ desires in some situations to be released with the district’s needs to protect investment in infrastructure and improvements. The result is a bill that provides a new, alternative procedure for release which would require release of land if requested by 100% of the landowners affected and if the landowners pay “just compensation” to the releasing district as determined by the board, or by a panel of appraisers if requested by the landowners. “Just compensation” is broadly defined to mean the value of the facilities and improvements located on the land to be released plus those that exist in whole or in part to serve that land. KRWA supports the bill as providing a reasonable compromise to a potentially explosive situation, and will be monitoring the bill throughout the Session.