

IN THE DISTRICT COURT OF THE FOURTH JUDICIAL DISTRICT OF
THE STATE OF IDAHO, IN AND FOR THE COUNTY OF ADA

CITY OF EAGLE, an Idaho municipal
corporation,

Plaintiff,

v.

EAGLE WATER COMPANY, INC., an Idaho
corporation,

Defendant.

Case No. CV01-19-03534

MEMORANDUM DECISION AND ORDER
ON MOTION TO DISMISS

I. INTRODUCTION

The City of Eagle brought this action for breach of contract and declaratory relief against Eagle Water Company, Inc., alleging the latter breached the two different provisions of the parties' Intertie Agreement. Eagle Water, joined by intervenor, Suez Idaho Water, Inc. ("Suez"), moved to dismiss the Complaint under IRCP 12(b)(6) on grounds that the Intertie Agreement is unenforceable under the statute of frauds. They also moved to strike the declarations of counsel for the City of Eagle.

Oral argument on the motion was held on August 28, 2019 after which the Court took the matter under advisement. The Court concludes that dismissal of the City's claims is not warranted by the statute of frauds.

II. STANDARD

Whether a claim should be dismissed under IRCP 12(b)(6) is a question of law. A court may grant a motion to dismiss for failure to state a claim under Rule 12(b)(6) only "when it appears beyond doubt that the plaintiff can prove no set of facts in support of [the] claim which would entitle [the plaintiff] to relief." *Colafranceschi v. Briley*, 159 Idaho 31, 34, 355 P.3d 1261, 1264 (2015).

The court must look only to the pleadings to determine whether a claim for relief has been stated. *Hammer v. Ribi*, 162 Idaho 570, 573, 401 P.3d 148, 151 (2017). A court may only

consider those facts appearing in the complaint, supplemented by those facts of which the court may properly take judicial notice. *Paslay v. A&B Irrigation Dist.*, 162 Idaho 866, 871–72, 406 P.3d 878, 883–84 (2017). Because a trial court considering a Rule 12(b)(6) motion to dismiss has no right to hear evidence—and judicial notice is merely a substitute for the conventional method of taking evidence to establish facts—“the court has no right to take judicial notice of anything, with the possible exception of *facts of common knowledge* which controvert averments of the complaint.” *Id.*, quoting *Hellickson v. Jenkins*, 118 Idaho 273, 276, 796 P.2d 150, 153 (Ct. App. 1990) (emphasis in original).

If extrinsic information outside the pleadings are submitted by a party on a Rule 12(b)(6) motion, the court is free to consider the information and convert the motion into one for summary judgment pursuant to IRCP 12(d), or decide the Rule 12(b)(6) motion on the allegations contained in the complaint alone. *Id.* In other words, a court can dismiss an action under Rule 12(b)(6) if it considers only the complaint, despite whether a party has submitted additional materials to the record.

All reasonable inferences must be drawn in favor of the non-moving party. *Id.* This issue is not whether the plaintiff will ultimately prevail, but whether—after drawing reasonable inferences in its favor—the plaintiff is entitled to offer evidence to support the claim. *Orthman v. Idaho Power*, 126 Idaho 960, 962, 895 P.2d 561, 563 (1995). A court must grant a Rule 12(b)(6) motion to dismiss when, even if every allegation in a complaint were true, the plaintiff would not be entitled to relief.

III. FACTS

Eagle Water Company, Inc. (“Eagle Water”) owns and conducts a water utility supply and distribution business in and around Eagle, Idaho. It is regulated by the Idaho Public Utilities Company (“PUC”). In 2008, Eagle Water was facing a water supply shortage that resulted in a moratorium imposed by the Idaho Department of Environmental Quality (“DEQ”) on new connections to its water system. Eagle Water was subject to a consent order and enforcement by DEQ and a show cause hearing before the PUC. Eagle Water needed a large supply of standby water to continue operating.

Faced with these circumstances, Eagle Water approached the City of Eagle (“the City”) about connecting to the City’s new water storage tank through an intertie for a standby water supply. In July of 2008, the City and Eagle Water entered into the Intertie Agreement under which the City

allowed Eagle Water to connect its distribution lines to the City's water tank in exchange for specific monthly payments. The Intertie Agreement provides, in part:

3.2 Cash Payment. In addition, [Eagle Water] shall pay [the City] a fee for the connection to the Storage Tank of \$10,000.00 per month commencing on the date the interconnection is completed and approved by the [DEQ].

4. Duration... If the Intertie continues past 18 months from the Commencement date, the Intertie Lease Cash Payment shall increase five percent (5%) and every 18 months thereafter.

As consideration for the City's commitments, Eagle Water granted the City a permanent Right of First Refusal ("ROFR") within the Intertie Agreement that provides:

6. Right of First Refusal. If [Eagle Water] determines to sell or convey all or any part of its Water System, which shall be deemed to include, but not be limited to, water rights, wells and other infrastructure, and receives a bona fide offer for this Water System, before making any agreement to sell all or any portion of the Water System, [Eagle Water] shall give notice to City stating [Eagle Water's] desire to sell and the amount and terms of such offer in detail. City shall have the exclusive right for 30 days after receiving such notice to provide Notice of Intent to Purchase the Water System or portion thereof to which such bona fide offer refers at the amount of said offer; provided, that if the third party offer is for a consideration other than cash, the City shall have the right to pay the fair market value of such consideration in cash.... For purposes of this Section 6, this Right of First Refusal applies solely to an '[Eagle Water] Change of Control Transaction', which means one or a series of transactions in which (i) all or substantially all of [Eagle Water's] Water System is sold to a third party, or (ii) there is a stock sale, merger, consolidation or similar transaction as a result of which said third party owns a majority of the outstanding voting and outstanding capital stock of [Eagle Water] or any successor owner of [Eagle Water]. This Right of First Refusal shall be permanent and shall survive any termination or other modification of this Agreement, save and except for a termination by the City other than for a non-cured default by [Eagle Water] per Section 7, below.

The "Water System" at issue in the ROFR is defined in the Intertie Agreement as Eagle Water's "water utility supply and distribution business." The Recitals to the Intertie Agreement further explain that Water System is located "in and around Eagle, Idaho." The ROFR adds that the Water System includes but is not limited to "water rights, wells and other infrastructure." There is no other description of the Water System in the Intertie Agreement. Beyond the

language of the ROFR, there is no reference to an external record or document providing a description of the Water System.

The interconnection contemplated under the Intertie Agreement was completed on July 22, 2008 and was approved by DEQ shortly thereafter. Eagle Water began making the required monthly payments in August of 2008. However, it has not made a monthly payment since May of 2009, leaving a significant balance.

Over the ensuing years, Eagle Water and the City had discussions about the City purchasing all or part of Eagle Water's Water System, but no agreement was reached. Unbeknownst to the City, in May of 2018, Eagle Water received a bona fide offer to purchase its Water System from third party, H2O Eagle Acquisition ("H2O"). H2O's offer was an "Eagle Water Change of Control Transaction" under the Intertie Agreement. Thus, Eagle Water was required under the Intertie Agreement to provide notice to the City stating the amount and terms of H2O's offer in detail. However, Eagle Water never provided the City with notice of the offer.

On November 15, 2018, Suez Idaho Water, Inc. ("Suez") and Eagle Water filed a Joint Application and Request for Modified Procedure with the PUC seeking approval of the sale of Eagle Water's Water System. It was at that time that the City learned that Eagle Water had entered into an agreement to sell its Water System to H2O and that H2O subsequently entered into an agreement with Suez purporting to sell or assign its rights to Eagle Water's Water System to Suez.

On January 14, 2019, the City sent Eagle Water a Notice of Default regarding: (i) Eagle Water's failure to comply with the ROFR, and; (ii) Eagle Water's failure to continue to make the monthly payments under the Intertie Agreement. In response, Eagle Water asserted the ROFR was unenforceable but did not address the monthly payments. On February 26, 2019, the City filed the instant suit against Eagle Water, asserting claims for breach of contract based on Eagle Water's failure to honor the ROFR and failure to make monthly payments, a claim for breach of the implied covenant of good faith and fair dealing, and a claim seeking a declaratory judgment regarding Eagle Water's obligations under the Intertie Agreement. By Order dated June 11, 2019, Suez was allowed to intervene in this suit.

IV. ANALYSIS

A. Motion to Strike

In opposing the motion to dismiss, the City submitted, through counsel's declaration, nearly 300 pages of various documents of which the Court "should" take judicial notice under IRE 201. These documents include documents filed with the Idaho Public Utilities Commission ("PUC") in the case of *Floating Feather Partners, LLC v. Eagle Water Company*, PUC Case No. EAG-W-08-01 (Decl. Berry, Exhs. A, B, D, F, H, K (July 26, 2019)); an order issued by the PUC in that case (*Id.* at Exh. E); a document produced in discovery in that case (*Id.* at Exh. G); Special Meeting Minutes from the Eagle City Counsel (*Id.* at Exh. C); City of Eagle Ordinance No. 415 (*Id.* at Exh. I), and; a Certificate of Public Convenience and Necessity No. 278 issued by the PUC in *In the Matter of Application of Eagle Ranch Water Co., Inc.*, PUC Case No. U-1116-1 (*Id.* at Exh. J).

Eagle Water and Suez seek to strike the declaration on grounds that the material cannot be considered on a motion to dismiss. The City argues that these documents were "referenced" in its Complaint and, therefore, can be considered without converting the motion into one for summary judgment.

The Court may only judicially notice a fact that is not subject to reasonable dispute because it is generally known within the trial court's territorial jurisdiction or can be accurately and readily determined from sources whose accuracy cannot reasonably be questioned. IRE 201(b). With the exception of perhaps Exhibits E, I and J, the documents provided do not satisfy this standard. Further, none of these documents were incorporated by reference into the Complaint such that the Court may consider them without converting the motion into one for summary judgment. IRCP 12(d). Therefore, the Court opts not to consider the documents and will decide the matter by reference to the Complaint and attached Intertie Agreement under the Rule 12(b)(6) standard. The motion to strike the affidavit is granted.

In addition, Eagle Water and Suez move to strike a second declaration submitted by the City's counsel that provides documents rebutting an unsupported statement in Eagle Water's briefing that the City was the drafter of the Intertie Agreement. Decl. Berry (Aug. 21, 2019). At oral argument, Eagle Water withdrew the statement, thus rendering the second declaration irrelevant. Although Eagle Water's withdrawal of the statement effectively renders the motion to strike the declaration moot, the Court has opted to decide this motion based on the Complaint

and Intertie Agreement alone and, therefore, will grant the motion to strike the second declaration.

B. The Statute of Frauds Does Not Mandate Dismissal.

Eagle Water and Suez contend that the ROFR is a grant of an interest in real property, i.e. the Water System, and, therefore, subject to Idaho's statute of frauds. I.C. §§ 9-503, 9-505(4). Arguing that the Intertie Agreement fails to adequately describe the Water System as required by the statute of frauds, they argue it is unenforceable. In response, the City argues primarily that the statute of frauds does not apply because the ROFR's focus is not the conveyance of an interest in real property but rather the conveyance of Eagle Water's corporate business that is triggered by a "Change of Control Transaction."¹

Idaho's real property statute of frauds applies to the sale, conveyance, grant or assignment of an interest in real property. I.C. §§ 9-503, 9-505(4). An agreement providing for a right of first refusal to purchase a particular parcel of land is considered under Idaho law to be an interest in land subject to the statute of frauds. *Nicholson v. Coeur D'Alene Placer Mining Corp.*, 161 Idaho 877, 882, 392 P.3d 1218, 1223 (2017). The statute of frauds requires that all such transfer agreements (1) be in writing; (2) be signed by the party to be charged; and (3) "contain a description of the property, either in terms or by reference, so that the property can be identified without resort to parole evidence." *Ray v. Frasure*, 146 Idaho 625, 628, 200 P.3d 1174, 1177 (2009).² If an agreement for the sale of real property fails to comply with the statute of frauds, it is unenforceable both in law and in equity. *Id.*

The threshold issue to determine here is whether the ROFR is a grant of an interest in real property, which would implicate the statute of frauds, or whether it is a grant of an interest in a business, which does not necessarily trigger the statute of frauds. In arguing the latter, the City relies on authority stating that the conveyance of an interest in a business entity does not trigger the real property statute of frauds even if the business assets include real property. This authority states, in relevant part:

¹ The City offers several alternative arguments in the event the Court finds the statute of frauds applies to the ROFR. However, given the Court's conclusion that the statute of frauds does not warrant dismissal of the claims, it need not consider these alternative arguments.

² Water rights are considered real property rights and agreements conveying an interest in water rights are subject to the statute of frauds. *Olson v. Idaho Dept. of Water Resources*, 105 Idaho 98, 101, 666 P.2d 188, 191 (1983).

It has generally been held that a contract to sell an interest in a firm is not within the real property provision of the statute, even though the firm owns real estate, although there is some contrary authority.

9 Williston on Contracts § 25:17 (4th ed.).

This issue has not been addressed by Idaho's appellate courts. Jurisdictions that follow this approach reason that the real property statute of frauds does not apply to agreements to sell corporate stock or partnership interests because stock and partnership interests are personal property, not real property. *See, e.g. Firth v. Lu*, 49 P.3d 117, 120 (Wash. 2002) (addressing the sale of stock); *Beach v. Anderson*, 417 N.W.2d 709, 712 (Minn. Ct. App. 1988) (addressing the sale of a partnership interest). As these cases explain, even if the assets of the business include real property, a sale of stock or of a partnership interest will not trigger the statute of frauds unless the agreement is for the actual conveyance of real property.³ Thus, if an agreement is not for the actual conveyance of an interest in real property, the statute of frauds will not apply even if the end result is an interest in land. *Firth*, 49 P.3d at 120.

While Idaho has not addressed this precise issue, it has long been the law that stock is personal property and, therefore, would not be subject to the real property statute of frauds. *State v. Dunlap*, 28 Idaho 784, 156 P. 1141, 1145 (1916). This is logical since the change of shareholders in a corporation does not affect title or ownership of the corporation's property.

A business can be conveyed not only by a stock sale, but also through an asset sale. To the extent those assets consist of real property, the statute of frauds would apply. *Burns v. Gould*, 374 A.2d 193, 198 (Conn. 1977) (recognizing that an agreement by a corporation to convey a corporate asset consisting of real property would be subject to the statute of frauds, but an agreement to transfer the stock of a corporation which owns an interest in real property is not); *Hoffman v. S V Co.*, 102 Idaho 187, 190, 628 P.2d 218, 221 (1981) (lot sale agreement under which corporation agreed to convey an asset consisting of real property is subject to statute of frauds).

Having concluded that an agreement to purchase a corporation through a stock sale would not be subject to the statute of frauds but an agreement to purchase corporate real estate

³ *See also*, 1 Fletcher Cyc. Corp. § 31 (2019 Update) ('The shares in a corporation that owns nothing but real estate are nevertheless mere personal property, since the shareholders are not the owners of the real estate, but the corporation alone is.')

assets would, the question next becomes whether the ROFR was for the former or the latter, or perhaps for something else. Because this issue involves the interpretation of a contract, the following principles apply:

When the language of a contract is clear and unambiguous, its interpretation and legal effect are questions of law. An unambiguous contract will be given its plain meaning. The purpose of interpreting a contract is to determine the intent of the contracting parties at the time the contract was entered. In determining the intent of the parties, this Court must view the contract as a whole. If a contract is found ambiguous, its interpretation is a question of fact. Whether a contract is ambiguous is a question of law. A contract is ambiguous if it is reasonably subject to conflicting interpretations.

Bakker v. Thunder Spring-Wareham, LLC, 141 Idaho 185, 190, 108 P.3d 332, 337 (2005).

The ROFR is a right of first refusal specific to the “Water System” which is defined in the Intertie Agreement as Eagle Water’s “water utility supply and distribution business.” Per the Intertie Agreement, the Water System “includes, but [is] not limited to, water rights, wells and other infrastructure.” Thus, the Water System is a business that owns real property assets.

The ROFR is triggered if there is a “bona fide offer for this Water System” which, as the ROFR further explains, means an offer for an “[Eagle Water] Change of Control Transaction.” A Change of Control Transaction is defined as “one or a series of transactions in which all or substantially all of [Eagle Water’s] Water System is sold to a third party, or (ii) there is a stock sale, merger, consolidation or similar transaction as a result of which said third party owns a majority of the outstanding voting and outstanding capital stock of [Eagle Water] or any successor owner of [Eagle Water].” Thus, the Change of Control Transaction—or bona fide offer—can take the form of an asset sale or a stock transfer.

A right of first refusal is defined as “[a] potential buyer's contractual right to meet the terms of a third party's higher offer.” Right of First Refusal, *Black's Law Dictionary* (11th ed. 2019). Here, the ROFR entitles the City to receive notice from Eagle Water stating the amount and terms of the proposed Change of Control Transaction in detail. Within thirty day after receiving such notice, the City must provide a notice of intent to purchase “the Water System or any portion thereof to which the bona fide offer refers at the amount of said offer.”

Thus, the terms of the proposed Change of Control Transaction inform the scope of the ROFR. If the proposal is for the transfer or sale of Eagle Water’s stock, the City would have to purchase all or part of the stock under the same terms. In such a scenario, Eagle Water would

still own the real property, but the City would own or control Eagle Water's stock—a transaction that would not be implicated by the statute of frauds. At the time the ROFR was executed, it was not known—nor could it have been known—what form the future proposed Change of Control Transaction would take. In short, the ROFR is a contract right to match an offer for a yet-to-be-determined future bundle of sticks, i.e., the property—real and/or personal—set forth in the proposed Change of Control Transaction. While this future bundle of sticks may ultimately come to include real property, the Court cannot conclude that the ROFR itself was an agreement for the sale of an interest in real property subject to the statute of frauds.

In addition, even if the ROFR contemplated solely a future asset sale, its plain language reasonably suggests that parties contemplated relying on the terms of the proposed Change of Control Transaction to supply the description of real property at issue. Namely, the ROFR does not expressly limit the “Water System” to the business assets held by Eagle Water at the time the ROFR was executed. Businesses buy and sell assets. The ROFR is only triggered if the sale of “all or substantially all” of the business is contemplated, indicating that minor assets—including a parcel of real property or water right—could be sold by Eagle Water without triggering the ROFR. Likewise, Eagle Water could have purchased other real property or water rights in the intervening period. Indeed, it was possible that none of the real property held by Eagle Water at the time the ROFR was entered would be part of the property ultimately affected by the proposed change of control transaction itself. Thus, the ROFR applies to Eagle Water's assets as they exist at the time of the proposed Change of Control Transaction, which could include assets that Eagle Water may have acquired in the intervening period. Likewise, the proposed Change of Control Transaction might not include any property that Eagle Water held at the time the ROFR was executed.

The statute of frauds requires that a sales agreement for real property “adequately describe the property so that it is possible for someone to identify ‘exactly’ what property the seller is conveying to the buyer.” *Ray*, 146 Idaho at 629, 200 P.3d at 1178. Real property cannot be adequately described where it is not known. Because the ROFR encompasses Eagle Water's future acquired assets, including real property, the property description requirement of the statute of frauds would be unworkable. At the time of the ROFR's execution, the parties could not reasonably know what Eagle Water's real property assets would be when Eagle Water received a future proposed Change of Control Transaction. Thus, it is reasonable to assume that if the

proposed Change of Control Transaction was, in fact, a proposed asset purchase, the City and Eagle Water intended to rely on the terms of the proposed Change of Control Transaction to provide the description of the real property assets.⁴

Finally, application of the statute of frauds under these circumstances does not advance its purpose. As long ago observed by the Idaho Supreme Court, the real property statute of frauds “was intended to ...preclude the possibility of titles becoming subject to the capricious memories of interested witnesses” and “guard against the frailties of human memory and the temptations to litigants and their friendly witnesses to testify to facts and circumstances which never happened.” *Dunn v. Dunn*, 59 Idaho 473, 83 P.2d 471, 475–76 (1938). It is intended to protect against fraud, not “as an escape route for persons seeking to avoid obligations undertaken by or imposed upon them.” *Russell v. Russell*, 99 Idaho 151, 153, 578 P.2d 1082, 1084 (1978). Eagle Water and Suez appear to be using the statute of frauds to avoid Eagle Water’s obligation to the City, not to protect themselves against the City’s fraud. This is not a situation where the City is arguing that Eagle Water promised them a right of first refusal on a certain ten acre parcel of land where, in reality, the parties agreed the right of first refusal would cover a different ten acre parcel. The plain language of the Intertie Agreement indicates the parties’ intent that the scope of the ROFR would be the portion of Eagle Water’s business as defined by the proposed Change of Control transaction. To hold that the ROFR is invalid because it did not explicitly describe Eagle Water’s real property assets—which may or may not have been then owned by Eagle Water and which may or may not have ultimately been within the scope of a future bona fide offer —would not be a rational application of the statute of frauds.

In sum, drawing reasonable inferences in favor of the City, the Court cannot conclude that the real property statute of frauds applies to the ROFR because the ROFR contemplated a stock sale or asset sale of Eagle Water’s business, the extent of which would be defined by some future offer. Thus, it was not an agreement for the conveyance of an interest in real property. Further, even if the ROFR applied to Eagle Water’s real property assets, a reasonable inference to be drawn is that the parties anticipated that the terms of the proposed Change of Control

⁴ The Court is not, at this time, concluding as a matter of law that the parties to the Intertie Agreement unambiguously intended that the future bona fide offer would supply the property descriptions for the real property assets. It is merely concluding that, based on the allegations of the Complaint and the Intertie Agreement, this is a reasonable and practical interpretation.

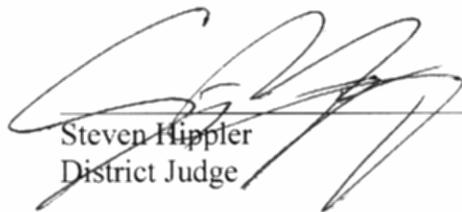
Transaction would supply the necessary real property descriptions to satisfy the statute of frauds. Consequently, dismissal of the City's claims is not warranted by the statute of frauds.

V. ORDER

Based on the foregoing, the Court DENIES Eagle Water and Suez's Joint Motion to Dismiss and GRANTS their motion to strike counsel's declarations.

IT IS SO ORDERED.

Dated this 18th day of October, 2019.


Steven Hippler
District Judge

CERTIFICATE OF MAILING

I hereby certify that on this 18th day of October, 2019, I emailed (served) a true and correct copy of the within instrument to:

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Clerk of the District Court

By: E. Child
Deputy Court Clerk

