

N.D.A.G. Letter to Dosch (Nov. 17, 1987)

November 17, 1987

Mr. Ronald M. Dosch
Devils Lake City Attorney
423 Sixth Street
P. O. Box 1048
Devils Lake, ND 58301

Dear Mr. Dosch:

Thank you for your letter of September 15, 1987, concerning the Devils Lake Steam Heat Plant. You inquire whether the Devils Lake City Commission may voluntarily dissolve the Devils Lake Steam Generation Corporation and the Devils Lake Steam Heat Authority. You further inquire as to whether the city of Devils Lake may incur any potential liabilities for the steam heat plant should both of these entities be dissolved.

Since your request of September 15, 1987, we have been in constant communication with you concerning your opinion request as to the facts involved in this particular matter. You have responded graciously by supplying additional information to us and by providing answers to our various questions. I appreciate your assistance and cooperation.

Because our responses to your questions are conditioned upon the facts as we understand them, I believe it is critical that we summarize those facts we assume to be correct for purposes of this response.

Prior to 1974, the Otter Tail Power Company operated a small, coal-fired steam plant in Devils Lake to drive turbines for electrical generation for local use. Turbines exhaust steam was sold locally to the city's business district through an underground steam distribution system. In 1974, Otter Tail closed the Devils Lake plant and shifted its operations to larger, more efficient plants. As part of the closing of the Devils Lake plant, Otter Tail conveyed the steam heat plant and distribution system to the city of Devils Lake. On either August 8 or 18, 1975, (both dates appear in the materials submitted to us) the city created the Devils Lake Municipal Steam Heat Authority ("Authority") pursuant to N.D.C.C. ch. 40-33.1. The purpose of the authority was to own, operate, and maintain the steam heat plant which was conveyed to the city of Devils Lake by Otter Tail Power Company. We assume that the Authority acquired all assets and liabilities of as well as title and interest to the steam heat plant.

In 1982, the Devils Lake Steam Heat Generation Corporation ("Corporation") was created. A year later, a bond series was proposed allowing the city of Devils Lake to acquire the business and assets of the Devils Lake steam heat plant from the Authority for the benefit of the Corporation.

Several events occurred in September of 1983. On September 15, a warranty deed was executed whereby the Authority conveyed to the city of Devils Lake the steam heat plant and all other structures, improvements, and fixtures relating thereto. The steam heat pipelines used in the steam heat system were also conveyed. On that same date, a lease was executed by the city of Devils Lake and the Corporation whereby the Corporation acquired the real estate as well as the existing improvements and personal property included in the steam heat system. On September 15, 1983, a bill of sale, assignment and assumption agreement was executed by the Authority and the Corporation. By this agreement, the Authority assigned its interests, rights and title in all properties used in connection with the steam heat plant to the Corporation except those assets and rights which were conveyed and assigned by the Authority to the city of Devils Lake in the warranty deed.

The Authority also appointed the Corporation as attorneys in fact for the Authority and the Corporation assumed the liabilities of the Authority. There was also an additional assignment between the Authority and the city of Devils Lake whereby the Authority assigned to the city all warranties, claims for breach of contract, rights against sureties, and other rights of the Authority arising out of construction contracts and surety bonds. Finally, on September 29, 1983, the Authority and the Corporation entered into a management services agreement. This agreement called for the Authority to provide general management services to the Corporation for the steam heat system. By this agreement, it was contemplated that the Corporation would not have any employees and that the Authority would operate the Corporation. As part of this agreement, it was stated that the Authority does not assume liability for any obligation or indebtedness of the Corporation.

In summary, it appears that the steam heat plant was originally the property and interest of the city of Devils Lake after Otter Tail conveyed it to the city in 1974. The steam heat plant then became the responsibility of the Authority in 1975. In 1983, the steam heat plant left the possession of the Authority and was transferred to the city of Devils Lake. The city leased the plant to the Corporation which, in turn, hired the Authority to run the steam plant on behalf of the Corporation. From these facts, it appears that the Authority had no interest in the steam heat plant after 1983 except in terms of the management services agreement whereby the Authority provided management services and actually operated the plant on behalf of the Corporation.

Your first question is whether the Devils Lake City Commission may voluntarily dissolve both the Corporation and the Authority pursuant to N.D.C.C. § 10-26-01. The statute provides for the voluntary dissolution of a nonprofit corporation by the board of directors of that corporation .

The Authority was created by action of the Devils Lake City Commission pursuant to N.D.C.C. ch. 40-33.1. The next-to-last sentence of N.D.C.C. § 40-33.1-02 provides for the termination of a steam heat authority and provides that the "corporate existence of the authority shall continue until all its liabilities have been met and until the existence of the authority is terminated by official action of the governing body." If the city desires to

discontinue the Authority, such action may occur by any official action of the governing body of the city. However, this section does require that the liabilities of the Authority must be satisfied before the Authority is terminated.

The Corporation is a nonprofit corporation and is subject to the voluntary dissolution procedures set forth in N.D.C.C. § 10-26-01. Those voluntary dissolution procedures, however, require action by the board of directors of the nonprofit corporation. Your letter indicates that there are no members of the board of directors of the Corporation and no individuals are currently interested in filling the vacancies existing on the board. Our review of the voluntary dissolution procedures for a nonprofit corporation has failed to reveal any procedure allowing for the voluntary dissolution of such corporation without action by the board of directors. Thus, it is my conclusion that the Devils Lake City Commission does not have the authority to cause dissolution of the Corporation on its own action and must rely upon action taken by the board of directors.

In a telephone conversation with this office, you have indicated the reluctance of many individuals to serve on the board of directors of the Corporation due to the potential liability that may occur. For your information, the 1987 Legislative Assembly has adopted a bill providing for limited immunity for directors of a nonprofit corporation. N.D.C.C. § 32-03-44 provides that a person who serves as a director of a nonprofit organization qualifying under a particular provision of the Internal Revenue Code is immune from civil liability for any act or omission resulting in damage or injury so long as the person acts in good faith and within the scope of his duties as a director. The statute further conditions the qualified immunity upon the absence of willful misconduct or gross negligence. The statute also prohibits the director from receiving reimbursement for or payment of expenses in excess of \$2,000 per year and prohibits the director from receiving compensation as payment for services rendered. You may wish to bring this statute to the attention of those individuals you approach in attempting to fill these vacancies.

Failing to fill the vacancies on the board of directors of the Corporation, the only alternative would appear to be a court supervised dissolution pursuant to N.D.C.C. § 10-26-10(2)(b). However, it is not known whether the creditors of the Corporation would be receptive to this alternative. This option may cause creditors to become uncooperative and of a desire to hold the city responsible for the debts of the Corporation.

Your second question concerns potential liabilities which may be incurred by the city of Devils Lake on behalf of the steam heat plant. By way of several telephone calls with this office, I understand this question to concern the liability of the city for unpaid debts or obligations of the steam heating plant. In your letter to this office of October 29, 1987, you indicated there are outstanding liabilities for withholding taxes and social security on employees who worked for the Authority. You also suggested possible real estate taxes due on the premises and lease payments due to the Burlington Northern Railroad for the land lease.

The answer to your question of whether the city may be responsible for any debts of either the Corporation or the Authority would depend upon the answer to the question who

is obligated to those creditors; the Corporation or the Authority?

Assuming it is the Corporation that may be obligated to one or more of the creditors, arrangements would have to be made with the creditors to satisfy the debts prior to the voluntary dissolution of the Corporation. Articles of dissolution may not be adopted by a corporation until all debts, obligations, and liabilities of the corporation have been paid and have been discharged, or where adequate provision has been made therefore. N.D.C.C. § 10-26-05(4). Assets of a corporation in the process of dissolution must be used in the satisfaction and discharge of all liabilities and obligations or for the making of adequate provisions for the satisfaction of such liabilities and obligations. N.D.C.C. § 10-26-02(1). Thus, the Corporation must make provisions for the adequate discharge of all its debts and obligations before it is allowed to voluntarily dissolve. Assuming that the creditors are in favor of voluntary dissolution, as is suggested by your letters, one would assume that arrangements as to how to satisfy such debts would be more likely to occur.

Assuming one or more of the creditors are the responsibility of the Authority, Devils Lake would not be liable for these obligations except in limited situations. Specifically, the liability of a city for the obligations of a steam heat authority is governed by N.D.C.C. § 40-33.1-11 which reads, in part, as follows:

40-33.1-11. State and city not liable on notes -- Exceptions as to cities. . . . The obligations of an authority shall not be a debt of a city and a city shall not be liable thereon unless a city agrees to assist in financing projects and facilities through the issuance of municipal bonds or other obligations which are considered to be a part of a the debt of the city as provided in section 40-33.1-04.

Our information is that city financing projects of 1983 were not considered a part of the debt of the city as provided for in N.D.C.C. § 40-33.1-04. Thus, the city of Devils Lake would enjoy protection from the debts of the Authority pursuant to N.D.C.C. § 40-33.1-11.

I hope this discussion is helpful to you and to the members of the Devils Lake City Commission in attempting to resolve this very difficult problem. If we can be of further assistance to you or to the city commissioners, please do not hesitate to contact us.

Sincerely,

Nicholas J. Spaeth

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