IN THE COURT OF APPEALS OF IOWA

No. 1-531 / 10-1968
Filed October 5, 2011

IOWA LAKES REGIONAL WATER,
Plaintiff-Appellant,

vs.

THE CITY OF OKOBOJI, DICKINSON COUNTY, IOWA and THE CITY OF ARNOLDS PARK, DICKINSON COUNTY, IOWA,
Defendants-Appellees.

Appeal from the Iowa District Court for Dickinson County, Don E. Courtney, Judge.

Iowa Lakes Regional Water appeals a district court's declaratory judgment ruling interpreting the provisions of a water purchase contract. **AFFIRMED.**

Donald J. Hemphill of Hemphill Law Office, P.L.C., Spencer, for appellant.

Ivan T. Webber and James R. Wainwright of Ahlers & Cooney, P.C., Des Moines, for appellees.

Heard by Eisenhauer, P.J., and Doyle and Mullins, JJ. Vogel, J., takes no part.

MULLINS, J.

This appeal concerns the proper interpretation of a water purchase contract entered into between Iowa Lakes Regional Water (ILRW) and the cities of Okoboji and Arnolds Park. In response to ILRW's petition for declaratory judgment, the district court determined that the water purchase contract limited ILRW to purchase a maximum of 200,000 gallons of water per day. ILRW appeals arguing the contract does not contain a maximum but rather permits it to purchase as many water allocations of 50,000 gallons per day as is necessary to meet the service needs of a specific ILRW territory. Upon our review, we affirm the well-reasoned ruling of the district court.

I. Background Facts and Proceedings.

In April 1977, the cities of Okoboji and Arnolds Park (Cities) entered into an Iowa Code chapter 28E agreement to provide for the joint construction, operation, and management of a potable water treatment and storage system designated "Central Water System." The agreement provided that the Cities would operate their own water distribution systems, and could sell water to other distribution systems only upon the Cities' joint authorization.

ILRW operates a potable water distribution system in Dickinson County. On October 8, 1991, the Cities, through Central Water System, entered into a "Water Purchase Contract" with ILRW (then known as Clay County Rural Water District). Under this contract, ILRW could pay Central Water System a "connection fee" based upon increments of 50,000 gallons per day. The agreement provided two options: ILRW could pay $45,000 for the first increment

with each subsequent increment costing $35,000, or ILRW could initially purchase two increments for $70,000 with each subsequent increment still costing $35,000. Under either option, if ILRW exceeded the increments already purchased during any five peak days during a calendar year, then it would be required to purchase an additional 50,000 gallons per day increment for $35,000. Despite this "connection fee" formula, the agreement stated that ILRW was "not to exceed 18,250,000 gallons per year" (or 50,000 gallons per day multiplied by 365 days). The agreement further included a designation of the ILRW service area to be served.[1]

ILRW initially purchased 100,000 gallons of water per day from Central Water Systems. However, in 1993, ILRW exceeded 100,000 gallons per day for five days and was charged $35,000 for an additional increment of 50,000 gallons per day. ILRW paid the additional charge, and was subsequently entitled to receive up to 150,000 gallons of water per day.

In 1995, it became necessary for Central Water Systems to make some capital improvements to its water treatment plant in order to comply with certain governmental rules and regulations. As a result of these improvements, ILRW and Central Water Systems negotiated and entered into a "Supplement and Amendment to Water Purchase Agreement" on February 20, 1996. The agreement set out ILRW's contribution amount for the capital improvements, and stated as follows:

> As [ILRW's] demand reached the amount of 150,000 gallons per day on three days during July, 1995, and as it is expected that

[1] This service area was revised by an amendment agreement in 1992.

> [ILRW's] demand may exceed 150,000 gallons per day on some days in 1996, [ILRW] agrees to pay [Central Water System], on or before December 31, 1995, the sum of $35,000.00. In consideration of this payment, [ILRW's] daily maximum shall be increased to 200,000 gallons per day from and after January 1, 1996.
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> The phrase "not to exceed 18,250,000 gallons per year" contained in subparagraph 1 of Section A of the water purchase contract is hereby amended to read "not to exceed 73,000,000 gallons[2] per year."

The agreement further provided that the October 8, 1991 agreement "remain[ed] in full force and effect" unless specifically amended or supplemented by the 1996 agreement.

In 1998, ILRW considered adding additional service territory in Dickinson County, and inquired if Central Water System would be interested in providing water to the new territory. The Central Water System Board denied any interest, and expressed their desire to remain within their current service area and protect any possible increase in production for the parties within the current service area.

The following year, ILRW began attempts to negotiate the purchase of additional increments of water from Central Water Systems. These negotiations were unsuccessful, and ILRW asserts the lack of success was because the Central Water System plant was operating at capacity, and therefore no additional increments of water were available for sale.

In 2007, Central Water Systems undertook a project to expand and modernize their facility. The project plans to expand the overall capacity of the water treatment plant, replace an aging raw water intake, incorporate a new membrane technology treatment process, and repair and rehabilitate worn

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[2] This amount reflects 200,000 gallons per day multiplied by 365 days.

components and features of the plant to accomplish various upgrades and to meet new anticipated water quality requirements. The costs of the project are projected to reach up to twelve million dollars.

When notified of the expansion, ILRW sought to purchase eight additional water increments of 50,000 gallons of water per day to raise its daily water allotment to 600,000 gallons. Although the plant expansion could meet ILRW's request for increased water increments, the city councils for Okoboji and Arnolds Park denied their request.

On May 7, 2009, ILRW filed a petition for declaratory judgment seeking interpretation of the amount of water it was entitled to purchase under the 1991 Water Purchase Contract and the 1996 Supplement and Amendment. ILRW contended that it had a contractual right to purchase as many 50,000 gallon water increments as was necessary to meet the needs of the agreed upon service area.[3]

Trial on the petition was held on August 18-19, 2010. On October 28, 2010, the district court determined the agreements limited ILRW to 200,000 gallons of water per day. ILRW appeals.

II. Standard of Review.

Our review of a declaratory judgment action depends on how the case was tried to the district court. *Van Sloun v. Agans Bros., Inc.*, 778 N.W.2d 174,

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[3] ILRW also sought a determination as to the amount or percentage share it was obligated to contribute for the proposed expansion and improvements. The district court adopted a formula requiring ILRW to contribute to the water quality and rehabilitation improvements, but not the capacity improvements. ILRW has not appealed this determination.

178 (Iowa 2010). This case was docketed as a law action, and was tried by ordinary procedure. *Okoboji Camp Owners Co-op. v. Carlson*, 578 N.W.2d 652, 653-54 (Iowa 1998). In addition, the case requests the interpretation of a contract, which is generally reviewed at law. *Van Sloun*, 778 N.W.2d at 178. Consequently, our review is for the correction of errors of law. *Harrington v. Univ. of N. Iowa*, 726 N.W.2d 363, 365 (Iowa 2007). The district court's findings of fact carry the force of a special verdict and are binding if supported by substantial evidence. *Van Sloun*, 778 N.W.2d at 179. However, we are not bound by the trial court's legal conclusions. *Id*.

III. Analysis.

ILRW argues that under the 1991 agreement it was given the ability to purchase additional 50,000 gallons per day increments with the only limitations being the needs of the specified territory and the capacity of the water treatment plant, and that nothing in the 1996 agreement amended this provision. Central Water Systems argues the 1996 Supplement and Amendment is clear and unambiguous allowing ILRW to purchase water "at such quality as may be required by [ILRW] not to exceed 73,000,000 gallons per year," with a "daily maximum" of 200,000 gallons per day. These two arguments require this court to participate in the process of interpretation by which we must determine the meaning of the words in a contract. *Fashion Fabrics of Iowa, Inc. v. Retail Investors Corp.*, 266 N.W.2d 22, 25 (Iowa 1978).

> The cardinal rule of contract interpretation is to determine what the intent of the parties was at the time they entered into the contract. Words and other conduct are interpreted in the light of all the

> circumstances, and if the principal purpose of the parties is ascertainable it is given great weight.

Pillsbury Co. v. Wells Dairy, Inc., 752 N.W.2d 430, 436 (Iowa 2008).

> "Any determination of meaning or ambiguity should only be made in the light of relevant evidence of the situation and relations of the parties, the subject matter of the transaction, preliminary negotiations and statements made therein, usages of trade, and the course of dealing between the parties. But after the transaction has been shown in all its length and breadth, the words of an integrated agreement remain the most important evidence of intention."

Fausel v. JRJ Enters., Inc., 603 N.W.2d 612, 618 (Iowa 1999) (quoting Restatement (Second) of Contracts § 212 cmt. b (1979)).

Upon our review, we agree with the district court and find the plain language of the 1996 agreement limits ILRW to 200,000 gallons of water per day. Although we agree with ILRW that the 1991 agreement possibly allowed for the purchase of additional increments of water without a daily maximum even though it had a yearly maximum, the 1996 Supplement and Amendment ended this possible anomaly by, in fact, supplementing and amending the 1991 contract. The plain language of the 1996 agreement states that ILRW had a "daily maximum" of 200,000 gallons. The agreement then amended the yearly maximum to correspond with this daily maximum, i.e. increase it to 73,000,000 which equals 200,000 gallons per day multiplied by 365 days.

In addition, we agree with the district court's finding that ILRW's purchase of additional water increments did "not establish a course of dealing sufficient to determine that ILRW could purchase additional units of water subject only to the capacity of the Central Water plant." Restatement (Second) of Contracts section 223 explains:

> (1) A course of dealing is a sequence of previous conduct between the parties to an agreement which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.
> (2) Unless otherwise agreed, a course of dealing between the parties gives meaning to or supplements or qualifies their agreement.

See also Iowa Code § 554.1303(2), (4) (providing similar definitions under the Iowa Uniform Commercial Code); *Dunn v. Gen. Equities of Iowa, Ltd.,* 319 N.W.2d 515, 516-17 (Iowa 1982) (setting forth both definitions).

The evidence simply shows that when ILRW's demand neared or surpassed its purchased increment amount, it entered into negotiations with Central Water System. In 1993 and 1996, Central Water System agreed to the increased increment amount in exchange for the payment of $35,000. In 1999 and 2007, Central Water System denied the requests. The 1996 negotiations were documented in the supplement and amendment, which clearly set new daily and annual maximum purchase provisions. The limited extent to which ILRW had previously been allowed to exceed the amounts set forth in the 1991 contract did not rise to the level of establishing a course of dealing sufficient to alter the written agreements. Even if that were so, the 1996 supplement and agreement set and clarified new maximums. *See* Iowa Code § 554.1303(5)(a) (stating that the express terms of an agreement and any applicable course of dealing must be construed whenever reasonable as consistent with each other, but if such a construction is unreasonable, then the express terms prevail over the course of dealing). Here, the only reasonable interpretation of the 1996 supplement and

amendment is to limit ILRW's purchase of water to a daily maximum of 200,000 gallons. Accordingly, we affirm the declaratory judgment of the district court.

AFFIRMED.