

**STRATEGIC PARTNERSHIP AGREEMENT
BETWEEN THE CITY OF CONROE TEXAS
AND
MONTGOMERY COUNTY UTILITY DISTRICT NO. 3**

THE STATE OF TEXAS §

COUNTY OF MONTGOMERY §

This STRATEGIC PARTNERSHIP AGREEMENT (this "Agreement") is entered into as of the Effective Date between the CITY OF CONROE, TEXAS, a municipal corporation principally situated in Montgomery County, Texas, acting through its governing body, the City Council of the City of Conroe, Texas (the "City"), and MONTGOMERY COUNTY UTILITY DISTRICT NO. 3 (the "District"), a political subdivision of the State of Texas created by the District Act (as defined herein) pursuant to Article XVI, Section 59, Texas Constitution and operating pursuant to the District Act and Chapters 49 and 54, Texas Water Code.

RECITALS

1. Texas Local Government Code, § 43.0751, as amended from time to time (the "Act") authorizes the City and the District to negotiate and enter into a strategic partnership agreement by mutual consent; and
2. The District lies entirely within the extraterritorial jurisdiction of the City. The City and the District have a mutual interest in the development of commercial property within the District and the improvement of the SH 105 corridor; and
3. This Agreement provides for the orderly full purpose annexation of the District and for the continuation of the District as a limited district following full purpose annexation; and
4. As required by the Act, the District held public hearings on _____, and on _____, at 15667 State Highway 105 West, Montgomery, Texas 77358 at which hearings members of the public were given the opportunity to present testimony or evidence regarding the proposed Agreement; and
5. As required by the Act, the City held public hearings on _____ and _____, at 300 West Davis Street, Conroe, Texas 77301, at which hearings members of the public were given the opportunity to present testimony or evidence regarding the proposed Agreement; and
6. Notice of the date, time, location and purpose of the public hearings was given in accordance with the Act, and the City and the District made copies of the proposed Agreement available in accordance with the terms of the Act; and

7. The City and the District wish to enter into a strategic partnership agreement to provide the terms under which services will be provided by City and the District upon full-purpose annexation and to provide other lawful terms that the Parties consider appropriate.

THE PARTIES AGREE AS FOLLOWS:

**ARTICLE I
FINDINGS**

The City and the District find and declare:

1. The recitals and the preamble to this Agreement are true and correct and are hereby adopted as findings of the City and the District.

2. The Act authorizes the City and the District to enter into this Agreement to define the terms under which services will be provided to the City and the District and under which the District will continue to exist after it is annexed pursuant to this Agreement;

3. This Agreement does not require the District to provide revenue to the City solely for the purpose of an agreement with the City to forgo annexation of the District;

4. This Agreement provides benefits to the City and the District, including revenue, services, or regulations that are reasonable and equitable with regard to the benefits provided to the other Party;

5. All the terms contained in this Agreement are lawful and appropriate; and

6. The City and the District negotiated this Agreement by mutual consent pursuant to the Act, after the City amended its three-year annexation plan to include the District.

**ARTICLE II
DEFINITIONS**

Unless the context requires otherwise, and in addition to the terms defined above, the following terms used in this Agreement will have the meanings set out below:

"Act" means Texas Local Government Code, § 43.0751 as amended from time to time.

"Agreement" means this strategic partnership agreement between the City and the District.

"Board" means the Board of Directors of the District.

"City" means the City of Conroe, Texas, a municipal corporation principally situated in Montgomery County, Texas.

"City Charter" means the Charter of the City and any amendments thereto adopted through the Effective Date.

"City Council" means the City Council of the City or any successor governing body.

"City Services" means the services provided by the City pursuant to Section 5.02 of this Agreement.

"District" means MONTGOMERY COUNTY UTILITY DISTRICT NO. 3, a conservation and reclamation district created pursuant to Article XVI, Section 59, Texas Constitution and operating pursuant to Chapters 49 and 54, Texas Water Code. The initial territory of the District is more particularly described in Appendix A attached hereto and incorporated herein by reference.

"District Act" means Chapter 8302, Texas Special District Local Laws Code, as it may be amended from time to time.

"District AV" means the total taxable value of all property in the District or otherwise subject to taxation by the District (including land, improvements, personal property, etc.), as certified for the District by the Montgomery Central Appraisal District (or its successor appraisal agency), plus an estimate of the value of any property under protest or otherwise not certified. The estimate shall be provided by the appraisal agency, but, in any event, the estimate may not be less than the owner's contention (or opinion) of value, as applicable. The District AV will be determined and updated from time to time, as provided in this Agreement. Notwithstanding the foregoing, the District AV will never be less than \$156,081,988, for purposes of this Agreement.

"Effective Date" means the date on which this Agreement is signed by the Mayor of the City following approval by the governing body of the City by ordinance (in a form acceptable to all Parties), but only if both of the following conditions are met prior to signature by the Mayor:

- (i) the governing body of the District must have approved this Agreement, and it must have been executed by the District, and
- (ii) the governing body of the Interconnected District must have approved a strategic partnership agreement with the City substantially similar to this Agreement, and that agreement must have been executed by the Interconnected District.

If either condition is not met prior to signature by the Mayor, this Agreement shall not take effect. If the signature by the Mayor does not occur, as provided above, by March 15, 2013, the Board of the District, with approval of the Board of the Interconnected District, may adopt a resolution to rescind its approval of this Agreement, in which case this Agreement shall not take effect.

"ETJ" means the extraterritorial jurisdiction of the City.

"Full Purpose Annexation Date" means December 31, 2014 (at 11:59 PM local time), the date on which the territory of the District is incorporated within the full purpose boundaries of the City pursuant to this Agreement.

"Government Code" means the Texas Government Code and any amendments thereto.

"Interconnected District" means MONTGOMERY COUNTY UTILITY DISTRICT NO. 4.

"Limited District" has the meaning given in the Act and in this Agreement refers to the status of the District during any period that it shall continue to exist following the Full Purpose Annexation Date, but subject to changes made by amendment to the District Act from time to time.

"Local Government Code" means the Texas Local Government Code and any amendments thereto.

"Non-conforming use" means any use of real property or any activity conducted upon such property that was lawfully permissible prior to the Full Purpose Annexation Date but would not be allowed subsequent to such date as a result of the application of any City ordinance, rule or regulation (if provisions allowing non-conforming uses to continue, etc. are disregarded).

"Non-conforming building or structure" means any building or improvement that conformed to all laws, rules or regulations applicable to the structure prior to the Full Purpose Annexation Date but that does not comply with the requirements of any City ordinance, rule or regulation made applicable as a result of annexation by the City (if provisions allowing non-conforming buildings or structures to continue, etc. are disregarded). "Party" or "Parties" means a party or the parties to this Agreement, being the City and the District.

"Service Plan" means the document entitled "City of Conroe Annexation Service Plan For Annexation Parcel 2014-02" (also marked "COMPILED DRAFT 2-7-2013" and "EXHIBIT B") which was prepared in connection with the annexation by the City of the District and filed with the City Secretary on February 9, 2013, as it may be amended from time to time with the approval of the City Council and the Board.

"Wastewater Treatment Plant" (or "WWTP") means the existing sewage treatment plant (with construction work in progress) serving both the District and the Interconnected District and located near Lake Conroe, south of SH 105, in Montgomery County, Texas.

Unless the context requires otherwise, terms specially defined in Appendix B have the same meanings elsewhere in this Agreement.

ARTICLE III GENERAL PROVISIONS

Section 3.01. Generally.

The Parties desire to provide for: (i) the orderly and predictable annexation of the land within the District into the City for full purposes so that each Party may develop both short and long-term financial plans based on the annexation date, and (ii) provision of services to the area after annexation.

Section 3.02. Property Taxes and District Liability for Debts of the City.

Prior to the Full Purpose Annexation Date neither the District nor any owners of taxable property within the District shall be liable for any debts of the City, and no ad valorem taxes shall be levied by the City upon taxable property within the District.

Section 3.03. Powers and Functions Retained by the District.

(a) During the term of this Agreement, the District is authorized to exercise all powers and functions provided by the District Act and any existing law or any amendments or additions thereto, except as expressly limited by this Agreement. The District's assets, liabilities, indebtedness, and obligations, including any obtained or incurred after the Effective Date, will remain the responsibility of the District, except for those to be transferred to the City under this Agreement.

(b) Without limiting the foregoing powers and functions, the District shall notify the City prior to the issuance of any bonds, certificates of obligation, re-funding bonds or other debts to be paid in whole or in part from a pledge of the ad valorem tax revenues of the District. Such notice shall be given at least twenty-one (21) days in advance of the proposed issue and shall include a substantially-complete copy of the preliminary official statement for the bonds. Not later than thirty (30) days following the issuance of the bonds the District shall provide City a copy of the official statement and the schedule of principal and interest payments for such bonds.

Section 3.04. Annexation of Additional Territory by the District.

No territory may be annexed to the District after the Effective Date of this Agreement without the prior written consent of the City and any such annexed territory shall also be subject to this Agreement. The owner of any property seeking annexation to the District must also consent to the annexation of the territory by the City and such consent to municipal annexation shall be a condition of City's consent to annexation by the District. If either party deems it necessary, this Agreement must be amended to cover the annexed territory. If, for any reason, annexation of such additional territory by the City is contested or held invalid or ineffective, neither this Agreement nor its application to other territory will be affected.

ARTICLE IV
RESERVATION OF WASTEWATER TREATMENT CAPACITY FOR CITY

Section 4.01. Wastewater Treatment Capacity Reserved for City.

(a) The District agrees to reserve for the City 150,000 gallons per day of treatment capacity from District's share of the total treatment capacity available from the Wastewater Treatment Plant, subject to Appendix B. The City intends by a separate agreement with the Interconnected District to reserve 150,000 gallons per day of treatment capacity from the Interconnected District's share of the Wastewater Treatment Plant capacity with the intent that total treatment capacity of 300,000 gallons per day be reserved for City, subject to Appendix B. Physical use of such capacity is subject to the provisions of Appendix B, including, for example, the requirement to provide advance notice.

(b) The City shall have the right, but not the obligation, to transfer all or any portion of its reserved capacity to a third party seeking service from the District or the Interconnected District. The City retains full discretion regarding payment and terms for any such transfer, including, for example, the discretion to require payment of impact fees (provided, however, any capacity transferred may not be further transferred or assigned). Upon notice to the District following any such transfer, the City Capacity (as determined in accordance with Appendix B) will be reduced by the amount of capacity transferred (in gallons per pay), and the City's annual Capacity Reservation Fee (as well as the annual actual-cost "true up" amount described below) will be diminished proportionately. See Section 4.04, below and Sections B2.05 and B3.02 of Appendix B. This provision shall not be construed to require the District to serve any such transferee upon terms or conditions other than: (i) those applicable to other customers of the District and (ii) provisions, if any, related to specific characteristics of the service requested or the transferee's proposed buildings and other improvements, including location, collection system, access, feasibility, quantity or composition of waste, etc. In addition, the District may require the transferee to pay a portion of the WWTP Expenses until all the transferred capacity is actually used to serve buildings and other improvements (or is formally released to the District or expires). If capacity is so transferred, and if some or all of the transferred amount is not actually used to serve buildings and other improvements before the third anniversary of the transfer, the District may recall the amount not actually used by: (i) notifying the transferee, and (ii) paying the transferee the amount of money (if any) paid by the transferee for the capacity transferred but not actually used (and payment may be allocated on a per-GPD basis). Any capacity so recalled reverts to the District.

Section 4.02. Consideration For Reservation of Treatment Capacity.

In consideration for the reservation of treatment capacity in the Wastewater Treatment Plant the City agrees to defray part of the District's debt service (incurred for the current expansion of the Wastewater Treatment Facilities), in accordance with the payment schedule and payment procedures shown in Appendix C.

Section 4.03. Prepayment, Re-financing, Etc.

The City shall have the option of pre-paying the debt service payments shown in Appendix C, at any time. In addition, if the City desires to re-finance all or part of such debt service and so notifies the District, the District agrees to cooperate and provide reasonable assistance to the City to effectuate a re-financing. Such cooperation and assistance could include, for example, calling some or all of the bonds for which the debt service was incurred. The City must bear the costs incurred by either party in connection with such a re-financing (proposed or completed) and must provide the cash needed to redeem any bonds that are called. Any debt service funds and reserve funds related to the District's bonds or debt service payments remain the property of the District.

Section 4.04. Capacity Reservation Fee.

(a) As additional consideration for the reserved capacity, and to provide for preserving and maintaining such capacity, the City shall pay to the Operating District (for deposit into the WWTP Account, for the benefit of both the District and the Interconnected District) an annual Capacity Reservation Fee due on October 30 of each year. Each Capacity Reservation Fee shall be paid in advance for the calendar year beginning on January 1 following the due date. The first Capacity Reservation Fee shall be due on October 30, 2014 for the calendar year 2015. The Capacity Reservation Fee is a percentage of the annual Non-Flow-Related WWTP expenses that is equal to the percentage of total WWTP Design Capacity that is reserved to the City. Initially the City's reserved capacity is equal to 25% of the Design Capacity.

(b) The Capacity Reservation Fee shall be paid based on the budget estimate of Non-Flow-Related WWTP expenses in the WWTP budget adopted by the Operations Committee for the upcoming calendar year and shall be subject to adjustment to actual cost ("true up") as hereinafter provided. The allocation factors shown in Section B4.02 of Appendix B shall be applied to determine the Non-Flow-Related WWTP Expenses.

(c) Beginning on April 1, 2016, and continuing on the first day of April of each subsequent year the Operating District shall calculate the actual-cost "true up" amount for the preceding calendar year, which will be the sum of:

- (1) any fee, service charge, penalty, tax or fine required to be paid by any government or regulatory authority as a direct result of serving the City; plus
- (2) any increase in WWTP Expenses triggered by an expansion triggered by the City, as provided in Section B2.04(h) of Appendix B; plus
- (3) a part of the Non-Flow Related WWTP Expenses (excluding items listed above) incurred during the preceding calendar year, such part being determined by the ratio of: (i) the average City Capacity during the preceding calendar year to (ii) the average Design Capacity during the preceding calendar year; plus
- (4) any other payments required by Appendix B or agreements entered into pursuant to Appendix B.

The Capacity Reservation Fee paid for such year shall be compared to such actual-cost "true up" amount for the year. If the Capacity Reservation Fee paid for such year exceeded the actual-cost "true up" amount for the year, then any such excess sum shall be promptly refunded to City. If such actual-cost "true up" amount for the year exceeded the Capacity Reservation Fee for such year, then City shall pay the difference within thirty (30) days of the receipt of an invoice for same from the Operating District.

(d) Beginning when the City first physically delivers sewage to the WWTP, the City shall receive regular monthly billings for Monthly Charges under Section B3.02 of Appendix B. These bills will include a portion of Flow-Related WWTP Expenses (and the other expense items specified in Section B3.02), and they shall be paid in accordance with Section B3.02 et seq. Charges for Non-Flow-Related WWTP Expenses shall not be included in the Monthly Charges (because they are to be covered by the Capacity Reservation Fees and the actual-cost "true up" amounts, as described above).

ARTICLE V SERVICES PROVIDED BY THE DISTRICT AND CITY

Section 5.01. District Services.

(a) District services are not affected by this Agreement until the Full Purpose Annexation Date. From and after the Full Purpose Annexation Date, the District shall provide the following:

1. *Water supply, transmission, distribution, etc.*

This includes "retail" water service for persons and properties now served by the District's water system, as it may be improved, extended and enlarged by the District, for: (i) areas within the District's boundaries and outside-District service areas, as they now exist and as they may be extended with consent of the City, and (ii) other areas approved by the City. This also includes water production, transmission, and compliance with groundwater reduction regulations.

The City and the District agree to cooperate to allow the District to deploy and use excess water supply available from the District to supply nearby areas in the vicinity of Lake Conroe. Such cooperation may include bulk purchases of available water by the City or other retail utilities for resale to the utility's customers, or the extension of water utility service by the District to other territory outside the District's boundaries or service areas, subject to the following:

- a. Extensions into the City's ETJ (and extensions of District facilities through or across the City's limits without providing retail service inside the City)

require consent of the City, but such consents may not be unreasonably withheld or delayed.

- b. Extensions to serve areas inside the City's limits require the City's consent.
- c. If City proposes new water service (or water sales) within City limits but near the District, the City and the District agree to meet and confer to consider possible use of District excess water capacity for that purpose, if available.
- d. Extensions of the District's groundwater reduction plan (without physical extension of water service) are allowed in any area.

This provision shall not be construed to obligate City to purchase water from District.

2. *Sanitary sewer service*

This includes "retail" sanitary sewer service for persons and properties now served by the District's sanitary sewer system, as it may be improved, extended and enlarged by the District, for: (i) areas within the District's boundaries and outside-District service areas, as they now exist and as they may be extended with consent of the City, and (ii) other areas approved by the City. This includes collection and transmission of wastewater to the Wastewater Treatment Plant where the District will treat and dispose of the wastewater. This also includes treatment and disposal services provided to City on a "bulk" or "wholesale" basis as provided by this Agreement.

3. *Solid waste collection and disposal*

This includes providing solid waste collection and disposal service for persons now receiving that service from the District as well as other similarly-situated persons within the District's boundaries, as they now exist or as they may be extended with consent of the City.

4. *Maintenance, repair, and replacement of storm sewer facilities*

This service includes maintaining, operating, repairing, and replacing storm sewer facilities now maintained by the District. This service also includes maintaining, operating, repairing, and replacing such facilities as they may be improved, extended, and enlarged by the District.

(b) Standards for District Services, Paying For Services, Etc.

The services described by this section must comply with the Service Plan. In providing each service, the District is responsible for providing all facilities, tools, equipment, supervision, goods, personal services and other items necessary or incidental to providing the service and for adopting rules and regulations governing such services, and the District will establish and collect fees and charges (in

addition to, or in lieu of, taxes) to pay for such services, all of which shall apply in lieu of similar provisions, rules, regulations, fees or charges of the City. In this regard, it also agreed that: (i) the District's water conservation and drought regulations shall apply to use of District services, in lieu of any City ordinances, rules and regulations otherwise applicable; and (ii) the District's plumbing regulations (relating to, for example, customer service inspections, cross-connections, etc.) shall apply in addition to City ordinances, rules and regulations affecting plumbing. The District and the City may work out arrangements for joint plan-checking, permitting and inspections of plumbing.

Section 5.02. City Services.

The City shall provide the following:

1. Payment for Services.

As provided by Section 43.0751(f)(3) of the Act and in consideration of the services to be provided by District under this Agreement (including, for example, maintaining, operating, repairing, replacing, extending and enlarging storm sewer facilities), the City agrees make an annual payment to the District. Each payment shall be made on or before February 15 of each year, from and after the Full Purpose Annexation Date, except that the City shall have the option of postponing the first payment from February 15, 2015 until August 15, 2015. The amount of the payment shall be \$60,000 plus \$0.05 per \$100 of District AV, determined as of the preceding December 31 (which means that the District AV would be based on appraisals and estimates for the preceding tax year).

In addition, City agrees to make certain payments to defray part of a lease-purchase obligation previously incurred by the District, in accordance with the payment schedule and payment procedures shown in Appendix D. City shall have the option of pre-paying such payments at any time. If City desires to re-finance all or part of such payments and so notifies the District, the District agrees to cooperate and provide reasonable assistance to the City to effectuate a re-financing. The City must bear the costs incurred by either party in connection with such a re-financing (proposed or completed) and must provide the cash needed. Any security deposits, reserve funds and similar funds paid by the District (and not defrayed by City payments) remain the property of the District.

2. Other Services.

From and after the Full Purpose Annexation Date, the City shall provide all other municipal services in accordance with the Act and the Service Plan. It is agreed and understood that property owner associations retain the discretion to continue providing certain functions and services, as indicated in the Service Plan.

Section 5.03. Application of Municipal Codes, Ordinances and Regulations.

(a) The following provisions govern the application of municipal regulatory provisions from and after the Full Purpose Annexation Date:

(1) Except as otherwise provided by this section, any non-conforming use may continue indefinitely provided that such use may not be materially expanded, including but not limited to materially increasing the area devoted to the use or adding materially to the hours of operation. A non-conforming use other than a seasonal use may not be reinstated after the use has been discontinued for a period of six (6) months or longer. A seasonal non-conforming use that occurs only periodically may not be continued unless the use has occurred at least once during the previous twelve (12) calendar months.

(2) A non-conforming building or structure may continue to be occupied, used and repaired without being conformed to the requirements of any City ordinance, rule or regulation that would otherwise be applicable, provided however any material addition or expansion to such building or structure shall conform to such requirements. Work done to accomplish a material repair or reconstruction of a non-conforming building or structure shall be done in conformance with such requirements, if applicable to such work when it is done. However, the entire building or structure would not have to be brought in to compliance unless: (i) the repair or reconstruction requires expenditures in excess of 50% of the value of building or structure under repair or reconstruction, and (ii) bringing the entire building or structure into compliance is expressly required by ordinance, rule or regulation in effect at the time. This section shall not be construed to relieve any person of the requirement of obtaining an applicable permit (but the requirements for issuing and enforcing such a permit shall conform to this section).

(3) Buildings and structures shall be categorized by use in accordance with the building codes of the City. After the Full Purpose Annexation Date if a building or structure is converted from one use type to another, the building (or part which is converted) must be brought into compliance with the code provisions that are: (i) applicable to the new use, and (ii) different from the code provisions applicable to the prior use.

(4) This section shall not be deemed to authorize the following activities in violation of an applicable municipal code, ordinance, rule or regulation after the Full Purpose Annexation Date:

- (i) the sale, use or possession of fireworks;
- (ii) outdoor fires or burning;
- (iii) the installation, operation or use of an alarm system subject to the permit requirements of City of Conroe Code of Ordinances Chapter 22, except that enforcement of such requirement for existing alarm systems shall not be commenced until April 1, 2015 to allow for the permitting of such existing alarm systems prior to the commencement of enforcement.

(5) As provided in Section 5.02(b) of this Agreement: (i) District rules, regulations, fees, and charges for services provided by the District shall apply in lieu of similar provisions, rules, regulations, fees or charges of the City; (ii) the District's water conservation and drought regulations shall apply to use of District services, in lieu of any City ordinances, rules and regulations otherwise applicable; and (iii) the District's plumbing regulations (relating to, for example, customer service inspections, cross-connections, etc.) shall apply in addition to City ordinances, rules and regulations affecting plumbing.

(6) Persons affected by a City ordinance, rule or regulation may pursue all available administrative remedies, including administrative interpretations, administrative approval to use alternate methods and materials, special exceptions, variances and waivers. The procedures and standards for such administrative remedies shall conform to this section.

(b) In addition, it is recognized that Local Government Code, Section 43.002 allows uses of land to continue (and new uses of land to begin) in certain circumstances, and they would not be subject to prohibition by the City. For purposes of that statute, the City and the District have determined that the "effective date of the annexation" would be December 31, 2014 and land uses lawfully in effect on such date will be considered a continuation of the manner in which the land was being used on the date annexation proceedings were instituted.

(c) The provisions described in subsection (a), above, have been adopted by the City ordinance authorizing this Agreement and will amend and control over all other ordinances, rules and regulations to the extent of any conflict or inconsistency. The City intends to keep such amendments in effect during the term of this Agreement, as a condition to performance under this Agreement by the District. If there is a proposal to repeal or alter such amendments, the City agrees to notify the District a reasonable time in advance and provide an opportunity for District representatives to meet and confer with City representatives regarding the proposal. Also, it is recognized that a repeal or alteration could affect the performance by the District of its obligations under this Agreement, in which case the District could raise the repeal or alteration as a defense in a proceeding to enforce such obligations.

(d) Real property covenants, conditions or restrictions applicable to real property within the District shall not be affected by annexation and may continue to be enforced according to their terms and provisions, and the City shall have no obligation for their enforcement.

Section 5.04. Other Programs and Projects.

On a case-by-case basis, the District and the City may agree to undertake other programs and projects jointly or cooperatively. For this purpose, it is recognized that the area within the District will become fully eligible for inclusion in the City's capital improvement programs. If either party proposes such a program or project, the other party agrees to meet and confer with respect to the proposal, provided that this provision shall not be deemed to obligate either party to undertake any such program or project.

ARTICLE VI FULL-PURPOSE ANNEXATION

Section 6.01. Full Purpose Annexation.

(a) The City shall not annex any part of the District with an effective date prior to the Full Purpose Annexation Date.

(b) On the Full Purpose Annexation Date the land included within the boundaries of the District shall be deemed to be within the full purpose boundary limits of the City without the need for any further action. From and after January 1, 2015, all taxable property within the territory of the District shall become subject to ad valorem taxation by the City.

Section 6.02. Conversion to Limited District; Expiration; Dissolution

(a) Upon the Full Purpose Annexation Date, the District shall become a Limited District and shall: (i) retain its current boundaries (as they may be extended by any annexations consented to by the City); (ii) be known by its current name and (iii) continue in existence for an initial term of ten years, subject to renewal by the governing body of the City. The City intends to renew the existence of the District for successive terms of ten years each until the District notifies the City that further renewals are not desired. However, if a change in law allows the District to continue to exist as a Limited District longer (or for renewal terms), each change shall be automatically incorporated into this Agreement, and the District shall continue to exist as long as allowed by law (or for as many renewal terms as allowed by law), until the District notifies the City that continued existence (or continued renewal) is no longer desired. If the Service Plan is not formally renewed beyond its original term, it shall continue to be enforceable as part of this Agreement until the Limited District is dissolved.

(b) While a Limited District, the functions of the District shall be as provided in the District Act and other provisions of state law.

(c) The Board of the District, with approval of the Board of the Interconnected District, may adopt a resolution to terminate this Agreement and dissolve itself. Unless otherwise consented-to by the City, the District must give notice to the City at least 180 days before the effective date of termination and dissolution. However, approval by the Board of the Interconnected District is not required if the District makes suitable arrangements to avoid any significant adverse effect upon the Interconnected District, and the Parties agree to work together to amend this Agreement or make other suitable arrangements to avoid any such effect on the Interconnected District. If the Interconnected District does not take similar action to terminate its strategic partnership agreement and dissolve itself, with the same effective date as the date set by the District, the Parties agree to work together to amend this Agreement or make other suitable arrangements to allow the Interconnected District to continue functioning.

(d) When the initial term and renewal terms of the District's existence expire (and any other continuation of the District's existence allowed by law has also ended), or when the District is dissolved, whichever first occurs, the Limited District shall expire and cease to exist, and the City shall:

- (1) take over all the property and other assets of the District,
- (2) assume all the debts, liabilities and other obligations of the District, and
- (3) perform all the functions of the District, including the provision of services

The District will execute, prior to dissolution, any and all documents reasonably requested by the City to evidence such transfer.

(e) Notwithstanding any other provision of this Agreement, the District may not, without the consent of City, be dissolved if the principal amount of all bonds, certificates of obligation or other debts payable from a pledge of the ad valorem tax revenues of the District ("tax debt") exceeds the applicable maximum shown in the chart below:

Calendar year during which effective date of dissolution is set to occur	Maximum tax debt outstanding on the effective date of dissolution*
2015	\$500,000
2016	\$1,000,000
2017	\$1,500,000
2018 and after	\$2,000,000

* Bonds for which debt service is to be defrayed by the City as provided in Article IV are not counted toward the maximum. Lease-purchase obligations for which payments are to be defrayed by the City pursuant to Article V are not counted toward the maximum.

The District may by resolution, with the consent of the Interconnected District, transfer the service obligations of the District to the City and may continue to exist thereafter for the restricted purposes of levying and collecting an ad valorem tax to pay interest and principal on the remaining tax debt of the District, and after such tax debt has been reduced so that it is less than or equal to an applicable maximum shown in the chart above, the District shall be deemed dissolved. While the District continues to exist for such restricted purposes, it will have only those powers and functions reasonably necessary to carry out those restricted purposes (including complying with state law and raising necessary revenues). Any such transfer of service obligations shall be irrevocable, and City shall thereafter be responsible for the delivery of all municipal services within the District as provided by this Agreement and the annexation Service Plan. This subsection (e) does not apply to voluntary termination and dissolution under Section 8.05, below.

Section 6.03. Legislation Regarding Renewal, etc.

The Parties agree to work together, and with the Interconnected District, to prepare and present proposed amendments to the Act, the District Act or other appropriate statutes to: (i) authorize continued existence of the District (as a Limited District under this Agreement) beyond the initial ten-year term until the District determines that continued existence is no longer desired, and (ii) to enhance provisions for enforcement of this Agreement. The Parties also agree to cooperate on presenting such amendments to the Texas Legislature with a joint request that they be adopted. This section remains in effect for each session of the Legislature until such amendments are adopted and become law.

**ARTICLE VII
ENFORCEMENT, BREACH, NOTICES
AND REMEDIES**

Section 7.01. Generally.

This Article provides for enforcement and dispute resolution procedures, including determinations of breach, notices, mediation, available remedies and related matters.

Section 7.02. Notice of District's Default.

(a) The City shall notify the District and the Interconnected District in writing of any alleged material failure by the District to comply with a provision of this Agreement, describing the alleged failure with reasonable particularity. The District shall, within thirty (30) days after receipt of the notice or a longer period of time as the City may specify in the notice, either cure the alleged failure or, in a written response to the City, either present facts and arguments in refutation or excuse of the alleged failure or state that the alleged failure will be cured and set forth the method and time schedule for accomplishing the cure. The Interconnected District shall have the same rights to cure or present facts and arguments (or statements).

(b) The City shall determine (i) whether a failure to comply with a provision has occurred; (ii) whether the failure is excusable; and (iii) whether the failure has been cured or will be cured by the District or the Interconnected District. The District shall make available to the City, if requested, any records, documents or other information necessary to make the determination.

(c) If the City determines that the failure has not occurred, or that the failure either has been or will be cured in a manner and in accordance with a schedule reasonably satisfactory to the City, or that the failure is excusable, the determination shall conclude the investigation.

(d) If the City determines that a failure to comply with a provision has occurred and that the failure is not excusable and has not been or will not be cured by the District or the Interconnected District in a manner and in accordance with a schedule reasonably satisfactory to the City, then the City may exercise applicable remedies under Section 7.04.

Section 7.03. Notice of City's Default.

(a) The District shall notify the City in writing specifying any alleged material failure by the City to comply with a provision of this Agreement, describing the alleged failure with reasonable particularity. The City shall, within thirty (30) days after receipt of the notice or the longer period of time as the District may specify in the notice, either cure the alleged failure or, in a written response to the District, either present facts and arguments in refutation or excuse of the alleged failure or state that the alleged failure will be cured and set forth the method and time schedule for accomplishing the cure.

(b) The District shall determine (i) whether a failure to comply with a provision has occurred; (ii) whether the failure is excusable; and (iii) whether the failure has been cured or will be cured by the City. The City shall make available to the District, if requested, any records, documents or other information necessary to make the determination.

(c) If the District determines that the failure has not occurred, or that the failure either has been or will be cured in a manner and in accordance with a schedule reasonably satisfactory to the District, or that the failure is excusable, the determination shall conclude the investigation.

(d) If the District determines that a failure to comply with a provision has occurred and that the failure is not excusable and has not been or will not be cured by the City in a manner and in accordance with a schedule reasonably satisfactory to the District, then the District may exercise applicable remedies under Section 7.04.

Section 7.04. Resolution of Disputes; Remedies.

(a) *Mediation.* If a dispute or disagreement arises out of this Agreement, the Parties agree to use reasonable best efforts to settle it in a just and equitable manner, recognizing their mutual interests, by following these steps:

(i) They will meet and confer within ten business days of a notice from either Party requesting such a meeting.

(ii) If a settlement is not reached at such meeting, each Party shall provide in writing to the other Party, within the next ten business days, a proposal for the resolution of the dispute, which proposal shall specifically recognize and address the other Party's position as explained at the first meeting.

(iii) Within approximately ten business days following the exchange of said proposals, the Parties will again meet and confer. If no settlement is reached, either Party may submit the matter for mediation, and both Parties will participate and try in good faith to settle. Unless they otherwise agree, the mediation will be administered by the American Arbitration Association under its Commercial Mediation Rules and in accordance with the Texas Civil Practices and Remedies Code.

Either Party may include the Interconnected District in the mediation. No Party will commence litigation or other adversarial legal proceedings arising out of this Agreement against the other Party without first attempting the steps required by this section. This does not prohibit a Party from commencing such proceedings to prevent the running of a statute of limitations or other tolling rule or to request an injunction or other equitable remedy to prevent immediate and irreparable harm, but the Party must continue pursuing the steps required by this section. A Party may pursue mediation under this subsection before, during or after the notice and cure procedures prescribed by Sections 7.02 and 7.03.

(b) *Breach; Remedies.* A Party may file suit in a court of competent jurisdiction in Montgomery County, Texas (subject to the requirement to mediate, as provided above), and seek appropriate relief at law or in equity, including actions under the Uniform Declaratory Judgment Act, equitable remedies (including, for example, specific performance, mandamus and injunctions) and actions for money damages. Recognizing the unique nature of public and governmental services, it is agreed that termination of this Agreement shall not be a remedy for breach.

Section 7.05. Contract for Goods and Services; Provisions For Payments.

As between the Parties, this Agreement shall be conclusively deemed to be a contract for the provision of goods and services to both the City and the District pursuant to Chapter 271, Subchapter I, Local Government Code. Each Party covenants and agrees to assess and collect user charges that will produce revenues sufficient to discharge its obligations to pay money under this Agreement, to the extent that other funds are not lawfully available for such purpose. The Parties understand that the City has discretion to use funds from user charges, from its regular tax levies, from sales taxes or from other lawful and available sources to discharge its obligations under this Agreement. If, for any reason, funds from such sources, taken in the aggregate, are not sufficient to discharge those obligations, the City must take all steps necessary to: (i) collect the special contract tax levied in connection with the approval of this Agreement and (ii) apply the proceeds from that tax to discharge its obligations under this Agreement, but only to the extent required.

**ARTICLE VIII
BINDING AGREEMENT, TERM,
AND AMENDMENT**

Section 8.01. Beneficiaries.

This Agreement binds and inures to the benefit of the Parties, their successors and assigns. The District shall record this Agreement with the County Clerk in the Official Records of Montgomery County, Texas. This Agreement binds each owner and each future owner of land included within the District's boundaries in accordance with Subsection (c) of the Act. There are no third-party beneficiaries of this Agreement unless specifically-named (e.g., Operating District, Interconnected District), and no un-named party shall have the right to sue to enforce this Agreement (whether based on tort, contract or other legal theory).

Section 8.02. Term.

This Agreement binds the Parties from and after the Effective Date. Provisions regarding services commence on the Full Purpose Annexation Date. This Agreement continues in effect until expiration or dissolution of the Limited District under Article VI, unless sooner terminated in accordance with the provisions of this Agreement

Section 8.03. Amendment.

The Parties by mutual consent, and with approval of the Board of the Interconnected District, may amend the terms of this Agreement at any time, but only by written instrument duly approved by the governing bodies of both Parties and duly signed by both Parties. However, approval by the Board of the Interconnected District is not required if the District makes suitable arrangements to avoid any significant adverse effect upon the Interconnected District, and the Parties agree to work together to amend this Agreement or make other suitable arrangements to avoid any such effect on the Interconnected District.

Section 8.04. Consolidation.

It is understood that the District may consolidate (or merge) with the Interconnected District, in accordance with state law. In that event, this Agreement shall continue in effect except for those provisions that cannot, as a legal or practical matter, be applied because of the consolidation or merger. The consolidated or merged entity shall be deemed to be the successor of the District.

Section 8.05. Other Voluntary Termination.

The Board of the District, with approval of the Board of the Interconnected District, may adopt a resolution to terminate this Agreement before the District becomes a Limited District. City has informed the District that in the event of such termination the City intends to annex the District for full purposes in December of 2014 in accordance with the City's previously adopted three-year annexation plan, and, as a result, the District would be abolished by operation of law. Unless otherwise consented-to by the City, the District must give notice to the City at least sixty (60) days before the effective date of such a termination. However, approval by the Board of the Interconnected District is not required if the District makes suitable arrangements to avoid any significant adverse effect upon the Interconnected District, and the Parties agree to work together to amend this Agreement or make other suitable arrangements to avoid any such effect on the Interconnected District. If the Interconnected District does not take similar action to terminate its strategic partnership agreement, with the same effective date as the date set by the District, the Parties agree to work together to amend this Agreement or make other suitable arrangements to allow the Interconnected District to continue functioning.

ARTICLE IX MISCELLANEOUS PROVISIONS

Section 9.01. Notice.

Any formal notices or other communications (Notice) required to be given by one Party to another by this Agreement shall be given in writing addressed to the Party to be notified at the address set forth below for the Party, (i) by delivering the Notice in person (ii) by depositing the Notice in the United States Mail, certified or registered, return receipt requested, postage prepaid, addressed to the Party to be notified, (iii) by depositing the Notice with Federal Express or another nationally recognized courier service guaranteeing next day delivery, addressed to the

Party to be notified, or (iv) by sending the Notice by telefax with confirming copy sent by mail. Notice deposited in the United States mail in the manner herein above described shall be deemed effective from and after the third business day following the date of such deposit. Notice given in any other manner shall be effective only if and when received by the Party to be notified. For the purposes of Notice, the addresses of the Parties, until changed as provided below, shall be as follows:

All Notices required or permitted under this Agreement shall be in writing and shall be served on the Parties at the following address:

City: City of Conroe
ATTN: City Secretary
P.O. Box 3066
Conroe, Texas 77305

Telefax address: (936) 522-3009

District: Montgomery County Municipal Utility District No. 3
1301 McKinney, Suite 5100
Houston, Texas 77010-3095

Telefax address: (713) 651-5246

The Parties may from time to time change their respective addresses, and each may specify as its address any other address within the United States of America by giving at least five days written notice to the other Party. If any date or any period provided in this Agreement ends on a Saturday, Sunday, or legal holiday, the applicable period for calculating the notice shall be extended to the first business day following the Saturday, Sunday or legal holiday.

Section 9.02. Time.

Time is of the essence in all things pertaining to the performance of this Agreement.

Section 9.03. Severability.

(a) If any part of this Agreement or of a substantially similar agreement with the Interconnecting District is found to be unenforceable, all other parts remain enforceable, but subject to reformation as provided below.

(b) Because the Parties mutually believe that all parts of those agreements are enforceable, a finding that a part is unenforceable would indicate that their belief is in error and that the Parties are mutually mistaken. Therefore, if a Party is (or will be) materially and adversely affected by a finding of unenforceability, that Party make seek equitable reformation of this Agreement. The Parties intend that reformation should restore a balance of rights and duties equivalent to the balance they anticipated when they entered into this Agreement.

Section 9.04. Waiver.

Any failure by a Party to insist upon strict performance by the other Party of any material provision of this Agreement shall not be deemed a waiver thereof or of any other provision hereof, and the Party shall have the right at any time thereafter to insist upon strict performance of any and all of the provisions of this Agreement.

Section 9.05. Applicable Law and Venue.

The construction and validity of this Agreement shall be governed by the laws of the State of Texas without regard to conflicts of law principles. Venue shall be in Montgomery County, Texas.

Section 9.06. Reservation of Rights.

To the extent not inconsistent with this Agreement, each Party reserves all rights, privileges, and immunities under applicable laws.

Section 9.07. Further Documents.

The Parties agree that at any time after execution of this Agreement, they will, upon request of the other Party, execute and deliver the further documents and do the further acts and things as the other Party may reasonably request in order to effectuate the terms of this Agreement.

Section 9.08. Incorporation of Appendices and Other Documents by Reference.

All Appendices and other documents attached to or referred to in this Agreement are incorporated into this Agreement by reference for the purposes set forth in this Agreement.

Section 9.09. Effect of State and Federal Laws.

Notwithstanding any other provision of this Agreement, the District shall comply with all applicable statutes or regulations of the United States, the State of Texas and City Charter provisions implementing such statutes or regulations.

Section 9.10. Authority for Execution.

The City certifies, represents, and warrants that the execution of this Agreement is duly authorized and adopted in conformity with the City Charter and City Ordinances. The District certifies, represents, and warrants that the execution of this Agreement is duly authorized and adopted by the Board.

[EXECUTION PAGES FOLLOW]

IN WITNESS WHEREOF, the Parties have executed this Agreement in multiple copies, each of which shall be an original, as of the date signed by the Mayor of the City of Conroe.

MONTGOMERY COUNTY UTILITY DISTRICT NO. 3

By: _____
President, Board of Directors

ATTEST:

Secretary, Board of Directors
Tax ID No. _____

CITY OF CONROE, TEXAS

By: _____
Mayor

ATTEST:

City Secretary

APPROVED AS TO FORM:

City Attorney

THE STATE OF TEXAS §
COUNTY OF MONTGOMERY §

This instrument was acknowledged before me this _____ day of _____, 2013, by _____, as President, and _____ as Secretary, of the Board of Directors of MONTGOMERY COUNTY UTILITY DISTRICT NO. 3, a political subdivision of the State of Texas, on behalf of said political subdivision.

Notary Public in and for the State of Texas

(NOTARY SEAL)

THE STATE OF TEXAS §
COUNTY OF MONTGOMERY §

This instrument was acknowledged before me this _____ day of _____, 2013, by _____, as Mayor, and _____ as City Secretary, of the City of Conroe, Texas, a Texas home rule municipality.

Notary Public in and for the State of Texas

(NOTARY SEAL)

After recording, return to: