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## TEXAS COMMISSION ON ENVIRONMENTAL QUALITY

*Protecting Texas by Reducing and Preventing Pollution*

April 16, 2012

FILE # AL-47018-12

I.D. # 47018

### VIA HAND DELIVERY

The Honorable Greg Abbott  
Attorney General of Texas  
Attn: Opinion Committee  
P.O. Box 12548  
Austin, Texas 78711-2548

**RQ-1054-GA**

Re: Utilization of Section 403.055 of the Texas Government Code to recover damages resulting from breach of a grant contract awarded under Chapter 386 of the Texas Health and Safety Code, the Texas Emissions Reduction Program (TERP).

Dear Attorney General Abbott:

This is a request for an opinion from your office as to the availability of the warrant hold process to the Texas Commission on Environmental Quality (TCEQ) as a means of enforcing compliance with certain grant agreements.

### Background

In accordance with Chapter 386 of the Texas Health and Safety Code, the TCEQ administers the Texas Emissions Reduction Program (TERP), which is designed to create monetary incentives for projects to improve air quality in designated counties that have fallen, or are in danger of falling, below certain air quality standards as determined by the Environmental Protection Agency (EPA). Since the inception of TERP in 2001, TCEQ has awarded over \$900 million in grant funding for over 15,000 individual grant activities through the execution of more than 9,000 grant contracts.

A TERP grantee may fail to comply with the program requirements and thus, materially breach the grant contract in a variety of ways. See enclosed brief for additional details. TCEQ's efforts to enforce compliance begin with informal measures designed to correct the grantee's failures. However, when TCEQ determines that a TERP grantee has not complied with their contractual requirements under their TERP agreement, a formal written demand letter and invoice is sent to the grantee requiring the return of grant funds paid based on the noncompliance. The amount demanded is subject to modification by the amount of performance that was successfully achieved before the breach of the contract. Failure to return the invoiced grant funds subjects the grantee to potential litigation. Overall, this process is both time and resource intensive given the number of TERP grants and grant activities.

Recently, the State Auditor's Office (SAO) conducted an audit of TERP. In the report from this audit, the SAO recommended that TCEQ promptly apply warrant holds to non-compliant grantees. See SAO Report No. 11-012, Chapter 3, December 2010.

## **Warrant Hold Statute**

Section 403.055 of the Texas Government Code prohibits payments to debtors and delinquents. The statute prohibits the Comptroller from issuing a warrant to a person who has been properly reported by a state agency in accordance with the statute. TCEQ must meet two fundamental requirements in order to properly report a debtor to the Comptroller for placement of a warrant hold:

First, under Tex. Gov't. Code § 403.055(f), the person reported by TCEQ must be indebted to the state or have a tax delinquency.

Second, under Tex. Gov't. Code § 403.055(g), TCEQ must first provide the person with an opportunity to exercise any due process or other constitutional or statutory protection that must be accommodated before the agency or the state may begin a collection action or procedure. The Comptroller is prohibited by this statute from investigating or determining whether a state agency has provided the appropriate due process or other protections of subparagraph (g).

## **Issues on which an opinion is requested**

In following SAO's recommendation, I respectfully request an opinion from your office on the following two legal issues:

1. Does TCEQ's formal written demand for restitution damages based upon an unadjudicated claim for breach of a grant contract issued under Chapter 386 of the Texas Health and Safety Code create a "debt to the state" for purposes of application of Section 403.055 of the Texas Government Code?
2. Does the TCEQ process for determination of the breach and amount of damages and demand thereof satisfy the due process requirements of Section 403.055(g), and if not, what extra due process protections may be necessary?

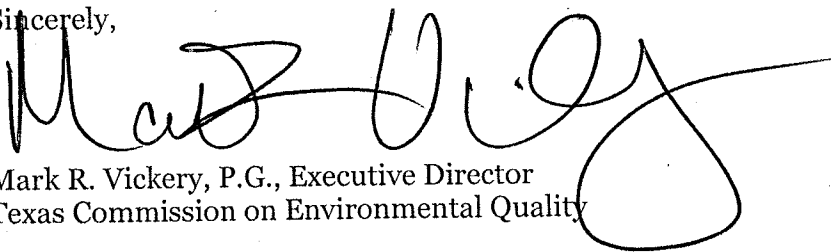
## **Background facts and attached briefing**

I have enclosed with this request a brief addressing these issues. It is provided to assist your office as it considers the questions presented by this letter. It does not make a recommendation on the substance of the opinion but rather discusses the issues TCEQ has identified in regards to the application of the warrant hold statute to these grant contracts.

## **Conclusion**

I appreciate your attention to this request. Thank you.

Sincerely,



Mark R. Vickery, P.G., Executive Director  
Texas Commission on Environmental Quality

Enclosure

cc: Zak Covar, Deputy Executive Director  
Stephanie Bergeron Perdue, Deputy Director, Office of Legal Services  
Caroline Sweeney, Special Counsel, Office of Legal Services  
Les Trobman, General Counsel  
Jim Harrison, Director, Intergovernmental Relations Division  
John Racanelli, Director, Financial Administration Division  
Joe Walton, Manager, Implementation Grants Section, Air Quality Division

## **Brief on application of Section 403.055 of the Texas Government Code for the recovery of grant funds awarded under the Texas Emissions Reduction Plan (TERP).**

This brief addresses the two questions raised by the April 13, 2012, request by the Executive Director of the Texas Commission on Environmental Quality.

### **I. Issues under consideration**

The issues raised by the questions presented in the April 13th opinion request concern whether the TCEQ may use the warrant hold process available under Section 403.055 of the Texas Government Code as a tool in recovering grant funds from low or non performing TERP grantees. The specific questions are:

1. Does TCEQ's formal written demand for restitution damages based upon an unadjudicated claim for breach of a grant contract issued under Chapter 386 of the Texas Health and Safety Code create a "debt to the state" for purposes of application of Section 403.055 of the Texas Government Code?
2. Does the TCEQ process for determination of the breach and amount of damages and demand thereof satisfy the due process requirements of Section 403.055(g), and if not, what extra due process protections may be necessary?

Although the scope of this request is limited to the breach of a TERP grant contract, the answer provided may be interpreted as allowing the use of the warrant hold process in other contractual settings, such as a state agency's procurement of goods and services.

The TCEQ will not present any conclusions on these issues, but rather will discuss the precedents leading to confusion on these issues.

### **II. Background**

The TERP program is created under Chapter 386 of the Texas Health and Safety Code. TERP awards grants for projects that create emissions reductions from trucks and other heavy equipment that are creditable to the State Implementation Plan required under the Federal Clean Air Act. The grant awards are based upon a calculated amount of emissions reductions resulting from a grantee's proposed new vehicle purchase, proposed old vehicle destruction, and committed future use of vehicle purchased with grant funding in designated areas of the state with air quality compliance issues.

The reduction is the product of the differential between the emissions rates of the old vehicle and new vehicle multiplied by the agreed annual usage of the equipment (usually expressed in miles) over an agreed term of years in the designated areas. This calculation is expressed in a total amount of emissions reduced over the life of the project expressed in tons of emissions reduced. The amount of grant funding provided is determined by the amount of emissions reductions created by the project.

In order to verify that the calculated emissions reductions paid for with grant funds are actually accomplished, the grantees are required to actually destroy the old vehicle, properly document the destruction of the old vehicle, use the new equipment in the amount and areas as agreed, and report twice a year on the usage of the new vehicle. The length of the reporting period depends upon the nature of the project and can have a duration from 5 to 15 years.

If the grantee fails to destroy or properly document the destruction of the old vehicle, fails to actually use the equipment in the amount proposed as proposed, fails to use the equipment in the designated areas, or fails to report on the required usage during the reporting period, then, by agreement, the proposed emissions reductions have not been achieved and grant funding is to be returned.

The TERP statute requires that the TERP grant contract incorporate provisions for recapturing grant money in proportion to any loss of emissions reductions projected in awarding the grant.<sup>1</sup> There are no special remedies, such as administratively enforceable fees or penalties, for enforcing the grant or recovering the grant funds.

### **III. Debt to the state**

The warrant hold statute itself does not contain a definition of debt to the state.<sup>2</sup>

In interpreting this statute, the Office of the Attorney General (“OAG”) has offered the following alternate definitions: “the article requires that a debt be established either by agreement between the state and the debtor; by the state’s proper allegation of the existence of a debt by statutory reference; or by some other lawfully effective means.”<sup>3</sup>

Conversely there is no authority to withhold warrants where there is a contrary statute, or where no “debt” exists in the usual and ordinary sense of the word.<sup>4</sup>

#### **A. Debt established by agreement**

The original language referring to this in Letter Advisory No. 57 reads as “establishment of a debt by agreement with the [debtor]”. Opinion No. MW-416 later paraphrased this as debt established “by agreement between the state and the debtor,”

In analyzing this factor, it is unclear what types of agreements would actually create a debt to the state. It may just apply to debt instruments, such as loans and promissory notes, which by their very nature create a debt by agreement. Or, in broader interpretation, could apply to any agreement between a person and the state where monetary damages are contemplated.

In discussing debt in application to Article 3912e § 7<sup>5</sup> the OAG discussed debt in terms of a similar warrant hold statute as follows:

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<sup>1</sup> Texas Health and Safety Code § 386.111(d). (d) Subject to availability of funds, the commission shall award a grant under this subchapter in conjunction with the execution of a contract that obligates the commission to make the grant and the recipient to perform the actions described in the recipient’s grant application. The contract must incorporate provisions for recapturing grant money in proportion to any loss of emissions reductions or underachievement in dispensing qualifying fuel compared with the volume of emissions reductions or amount of fuel dispensed that was projected in awarding the grant. Grant money recaptured under the contract provision shall be deposited in the fund and reallocated for other projects under this subchapter.

<sup>2</sup> Texas Government Code 403.055 was formerly codified as Article 4350 Vernon’s Codified Texas Statutes. For purposes of this section the language regarding indebtedness to the state is identical.

<sup>3</sup> Tex. Att’y Gen. LA-57 (1973), as cited in Tex. Att’y Gen Op. No. MW-416 (1981).

<sup>4</sup> Tex. Att’y Gen Op. MW-416 (1981), citing Tex. Att’y Gen Op. Nos. O-4655 (1942), O-5249 (1943).

<sup>5</sup> Article 3912e § 7 codified as Section 154.025 of the Texas Local Government Code (Disbursement to Persons with Outstanding Debt Prohibited).

Black's Law Dictionary, 4<sup>th</sup> Ed., defines the word "indebtedness" as "the owing of a sum of money upon a certain and express agreement." The word "debt" is defined as "a sum of money due by certain and express agreement; as by bond for a determinate sum, a bill or note, where the amount is fixed and specific and does not depend on any subsequent valuation to settle it."<sup>6</sup>

These opinions strongly suggest that "debt" is only established by specific agreement with a defined sum of money, such as debt instruments. By contrast, the TERP grant agreements are not so well defined. Grant funds are required to be returned, but only after a failure to perform the activities required by the grant — an amount based upon the subsequent valuation of the calculated cost of the contract breach. The requirement for the return of grant funds arises from the breach of the required grant activities; it is itself not the performance envisioned by the parties to the grant contract.<sup>7</sup>

### **B. Debt established by statutory reference**

The statutorily provided remedy for the TERP program is the requirement that the TERP grant contract contain provisions for funds recovery.<sup>8</sup> This does not create a fee or penalty that may be assessed, just a mechanism where funds may be recovered through an action in contract.

Compare this with a situation where the OAG has held that a debt was created by statutory reference. Opinion No. DM-217 (1993) discussed whether the Texas Surplus Property Agency could place a warrant hold on persons who failed to pay a service and handling fee. Where the relevant statute authorized the Agency to impose a fee, the failure to pay the fee created a debt to the state. The payment obligation was specifically imposed by statute and failure to remit the payment created a debt to the state.

Also compare with Chapter 391, Texas Health and Safety Code. This is the New Technology Implementation Grant Program which is administered by TCEQ and is funded out of the TERP plan. This program requires that reviews of the grants be performed by the Office of the Comptroller, and that any findings of misuse of grant funds expressly creates a debt to the state for the purposes of the warrant hold statute.

### **C. Other lawfully effective means**

The OAG offered this explanation of "other lawfully effective means:" "We would conclude, in this instance, that the debt must first be established by a lawfully effective means, *e.g.*, become an established legal obligation, by which is meant such obligation as would form the basis of a judgment in the

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<sup>6</sup> Tex. Att'y Gen. Op. No. WW-1504 (1962).

<sup>7</sup> Attached as Appendix A to this brief is a selection of the contractual provisions listing which, if breached, may require the return of grant funding, the provisions for calculation of liquidated damages, and listed contractual remedies. The entire TERP grant contract is attached as Appendix C.

<sup>8</sup> 386.111(d), see footnote 1 for text.

court of competent jurisdiction.”<sup>9</sup> This implies that the debt need not necessarily be established by an actual court judgment.

However, in interpreting a similar warrant hold statute at the county level, the OAG held that a delinquent tax, not yet confirmed by a judgment, is not a “debt” sufficient to apply the warrant hold.<sup>10</sup> The OAG relied heavily on previous opinions in finding that delinquent tax is not a debt “in the ordinary sense of the word” and reiterated the concerns expressed in Opinion O-1089, “[I]n holding up money which the county owes to an individual, who is a delinquent taxpayer, a county auditor would be, in effect, acting as a judge and jury over said taxpayers’ liability for the tax.” In other words, the OAG was concerned that, without any sort of process, a governmental decision maker may arbitrarily determine that debt exists and withhold other funds accordingly.

In the case of a breach of contract, these opinions suggest that a judgment or some other definite basis is needed to establish that the contract breach has in fact occurred and that the monetary damages are warranted in order before treating the damages as a debt, so that state funds aren’t arbitrarily withheld due to an agency’s decision on a contract breach.

In reviewing the three different sources of the establishment of a debt to the state, it is unclear whether the claim for return of TERP grant funds based upon the agency’s determination that the grant contract terms have been breached has been established either by agreement, by statutory reference, or by other lawfully effective means.

#### **IV. Due Process concerns**

In 1999, the Legislature added the due process language to Section 403.055(g).<sup>11</sup>

Prior to this amendment, the OAG discussed the legal inability to place warrant holds upon retirement benefits for former employees that have defaulted on Hinson-Hazelwood student loans.<sup>12</sup> The OAG stated as follows in regards to any future legislative attempts to place warrant holds on benefit payments:

Should the Legislature find this result unfortunate and desire to remedy it, it may of course do so. We caution, however, that any such legislation must consider the question of due process. A salary or retirement warranty is valuable property, and the Fifth and Fourteenth Amendments to the United States Constitution require that such property not be taken without due process of law. The requirement of due process is that a deprivation of this nature must “be preceded by notice and opportunity for hearing appropriate nature to the case.” *Mullane v. Cent. Hanover Bank & Trust Co.*, 339 U.S. 306, 313 (1950). What process may be due in a particular

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<sup>9</sup> Tex. Att’y Gen Op. MW-416 (1981) page 3.

<sup>10</sup> Tex. Att’y Gen Op. No. JC-0087 (1999).

<sup>11</sup> Acts 1999, 76<sup>th</sup> Leg. Ch. 1467 § 1.15.

<sup>12</sup> Tex. Att’y Gen. Op. No. DM-419 (1996).

case was generally adumbrated by the Supreme Court in *Matthews v. Eldridge*, 424 U.S. 319, 334-35:

*[I]dentification of the specific dictates of due process generally requires consideration of three distinct factors: First, the private interest that will be affected by the official action; second, the risk of an adverse deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards; and finally, the Government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirement would entail.*

The *Matthews* yardstick is a flexible one. The United States Court of Appeals for the Fifth Circuit has on occasion found that even informal procedures are sufficient to meet due process requirements. See *Nimon v. Resolution Trust Corp.*, 975 F.2d 240, 247 (5<sup>th</sup> Cir. 1992). However, we believe it would be most prudent for the legislature, should it decide to address this matter by statute, to include notice and hearing requirements in the statute as well.

In amending Section 403.055 the Legislature did not add any specific notice or hearing requirements as suggested by the OAG. The language added an agency may not place a warrant hold “unless the agency first provides the person with an opportunity to exercise any due process or other constitutional or statutory protection that must be accommodated before the agency or the state may begin a collection action or procedure.”

This has left the application of the factors of *Matthews* up to the individual agencies seeking to place a warrant hold.

In terms of the private interest involved in applying warrant holds to TERP grantees, the private interest most likely to be affected by this action will be the right to payment under contracts with the state.<sup>13</sup> Due to the nature of the business interests that usually apply for TERP grants it may be assumed that these grantees may, in the future be employed by other agencies of the State in road construction or other similar types of public works projects. As there would be a warrant hold in place, the Comptroller may withhold payments for work performed under these other unrelated contracts to satisfy the amount claimed as damages under the TERP contract.<sup>14</sup>

The procedures presently used to establish the amount owed under the TERP grants are the procedures outlined above with letters demanding cure followed by a final letter demanding the return of grant funds.<sup>15</sup> These letters explain the deficiency in the grantee's performance and the steps necessary to cure the performance and contain adequate time for the grantee to come into compliance. The letters contain notice that

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<sup>13</sup> Payment for persons performing under state contracts has been shown to be a Legislative priority by the passage of statutes protecting state contractors and subcontractors, such as the Prompt Payment Act, Chapter 2261 of the Texas Government Code, and the MacGregor Act, Chapter 2253 of the Texas Government Code.

<sup>14</sup> See Comptroller document APS 028, Reporting of State Debts and Hold Offset Procedures. “The Comptroller's office is authorized to offset state payments against a person's state debt.”

<sup>15</sup> Two examples of these final demand letters are included as Appendix B to this brief.

failure to perform may result in legal action being taken by the State and that a warrant hold may be placed upon them as a result of non-performance / non-payment.

Additional procedural safeguards above the existing system would involve the hearing of the issue before a neutral party through a lawsuit, administrative hearing, or other similar dispute resolution procedure.<sup>16</sup> Due to the amount of cases prospectively anticipated, such a system will be very time consuming and expensive.

## **V. Conclusion**

The TCEQ is committed to implementing the warrant hold system as recommended by the SAO, but is duly concerned that it is implemented properly to protect the constitutional interests of the TERP grantees and to protect the TCEQ from litigation if performed improperly.

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<sup>16</sup> The agency rules for processing contract disputes under Chapter 2260 of the Government Code specifically exempt grants from the process. *See* 30 Texas Administrative Code § 11.102(b)(8).