



# CITY OF HOUSTON

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May 17, 2023

The Honorable Charles Schwertner  
Chairman, Senate Committee on Business & Commerce  
P.O. Box 12068  
Austin, TX 78711

Re: Opposing House Bill 2265

Dear Chairman Schwertner and Members of the Committee,

My name is Daniell Davis. I am a Senior Assistant City Attorney for the City of Houston. I testify with the City's full authority to speak on its behalf as a part of my role and responsibilities. On behalf of the City of Houston I offer the following information in opposition of House Bill 2265 for the Committee's consideration as it contemplates legislation relating to the award of compensatory damages caused by certain governmental delays under governmental construction contracts.

This bill proposes an addition to Texas Government Code Chapter 2252 "Contracts with a Government Entity" by adding section 2252.909, "Compensatory Damages Caused by Governmental Delays in Construction Contracts" which states that a construction contract between a governmental entity and a contractor is prohibited from including any provisions barring the award of compensatory damages to the contractor for a delay to the extent the delay is caused solely by the governmental entity or by a party for which the governmental entity is responsible. The Section may not be waived and a purported waiver of the section is void.

The City's argument in opposition to HB 2265 is trifold. In short, it violates federal, state and local law. At the federal level HB 2265 directly contradicts federal procurement and cost principal requirements set forth in the Code of Federal Regulations which governs grantees and subrecipients under grants awarded by the U.S. Department of Housing and Urban Development ("HUD") such as the Community Development Block Grant and Disaster Recovery Grants. In addition, the bill violates state law by violating Article XI, Section 5 of the Texas State Constitution which prohibits City's from creating unfunded liability. Lastly this bill restricts the City's rights as a home rule municipality to do

anything authorized by its charter that is not specifically prohibited or preempted by the Texas Constitution, state or federal law.

### **Federal Law**

Over 30 grant programs administered by HUD are required to comply with the cost principles laid out in 2 CFR 200<sup>1</sup>. In 2022 alone, HUD awarded over \$451,000,000 in federal financial assistance to grantees in the State of Texas<sup>2</sup>, many of which are Government Entities. The City of Houston prioritizes the development of affordable housing, public facilities, infrastructure and disaster mitigation efforts, specifically flood mitigation projects. The City's success in administering these initiatives is directly tied to its access to HUD dollars. All grant, loan, developer and subrecipient agreements as well construction contracts that the City enters into utilizing federal funds are subject to the cost principals and procurement requirements set forth in 2 CFR 200 which expressly state that contracts shall be for a fixed price. Strict budget, reporting and compliance provisions leave no room for any federal funds to be unaccounted for at the onset of the Project. Additionally, 2 CFR 200.441 says that fines, penalties, damages and other settlements for a Grantee's violation of, or alleged violation of, federal, state or local laws are unallowable. HB 2265 would require the City to include in its construction contracts a provision for delay damages that carries with it an unpredictable compensatory damage amount. This violation could result in significant financial consequences for the City and indirectly affect the City's residents. If HUD finds the City is violating the terms of the grant agreements and not adhere to the federal rules and regulations they could require the City to repay the grant funding and/or prohibit the grantee from receiving future awards. Without HUD grant awards the City of Houston and all Texas entitlement recipients, state recipients and grant recipients that qualify as a government entity under 2252.909 would be at risk of losing much of the \$451,000,000 that goes to projects that provide benefits to our states most vulnerable communities.

### **State Law**

Unfunded liabilities are portions of a construction project in which the City has not designated or earmarked funding for or has not otherwise secured financing to cover the costs. Article XI, Section 5 of the Texas State Constitution provides that "no debt shall ever be created by any city, unless at the same time provisions be made to assess and collect annually a sufficient sum to pay the interest thereon and creating a sinking fund of at least two percent". In essence, this provision forbids a City from entering into a construction contract with a provision that could create a debt in which the City has no funding set aside to cover it. In *T. & N. O. R. R. Co. v Galveston County*, 169 S.W. 2d 713 (Tex. 1943), three railroad companies asserted that the indemnity agreement within their construction contract with Galveston County shielded them from liability from death claims resulting from wrongful death claims. The railroad companies contracted with Galveston County for the construction of a causeway, overwater railway and a drawbridge to connect Galveston Island with the mainland. The railroad was tasked with overseeing the operations of the drawbridge. One night, the railroad company accidentally left the drawbridge up and an unsuspecting car drove off the causeway into Galveston Bay killing the passengers. The Supreme Court held that "public policy demands that definite limitations be placed on the power of

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<sup>1</sup> [2022 Compliance Supplement \(whitehouse.gov\)](#)

<sup>2</sup> [Awards and Allocations - HUD Exchange; Book 1](#)

political subdivisions and the government to spend public money.”<sup>3</sup> The Supreme Court went on to cite Article XI, Section 5 and defined debt as used therein as “any pecuniary obligation imposed by contract, except such as was, at the time of the agreement, within the *lawful* and *reasonable* contemplation of the parties, to be satisfied out of the current revenues for the year or out of some fund then within the immediate control of the county.”<sup>4</sup> The Court found that if “the obligation does not arise as an item of ordinary expenditure in the daily functioning of the government or if it is not to be paid out of funds then in the county treasury, it is a debt and falls under the condemnation of the Constitution, unless the required provision for its payment is made at the time the obligation is incurred<sup>5</sup>. In accordance with the Constitution, the court determined the indemnity clause void.

Compensatory damages cannot be contemplated at the time the parties enter into the contract. Delay damage provisions in government construction contracts are customarily provisions that grant the government entity grounds to seek damages against a contractor. Delay claims against government entities are not “ordinary expenditures” and causes for possible delays throughout the project cannot accurately be predicted at its onset. In addition, compensatory damages are not able to be ascertained at the time the parties enter into the contract. HB 2265 penalizes the City for being good stewards of taxpayer money and opens the door for liability that cannot be budgeted for. The Court found in *T. & N. O. R. R. Co.* that public policy demanded “definite limitations on a political subdivision’s power to spend public money.” HB 2265 contradicts this notion in its entirety. The financial impact on the City’s construction costs could potentially be significant and come at the expense of the taxpayers. If this bill becomes law, any delay could potentially cause the City to incur thousands to millions in financial damages that could have been used to benefit the public.

### **Local Law**

Finally, HB 2265 restricts the parties right to contract. Parties to construction contracts often agree to damages, penalties or the lack thereof at the onset of a project in order to keep costs predictable. The City works with non-profit and for profit entities, many of which are small business owners and Low-Mod Income themselves. Prohibiting the parties from being able to contractually forego damage clauses is contrary to the fundamentals of contract law. The City of Houston is a home rule municipality which means is free to do anything authorized by its Charter that is not specifically prohibited or preempted by the Texas Constitution, state or federal law. Enacting HB 2265 would infringe on the City’s current rights by forcing it to comply with the new state law instead of governing itself.

The City is steadfast in its commitment to the residents of the City of Houston. HB 2265 carries with it significant concerns as it is in direct contradiction to federal and state laws and infringes upon the City’s current freedom to govern itself. The bill could have significant financial consequences that would ultimately affect Texans statewide. For the reasons stated above, the City of Houston respectfully opposes HB 2265.

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<sup>3</sup> *T. & N. O. R. R. Co. v Galveston County*, 169. S.W. 2d 713 (Tex. 1943)

<sup>4</sup> *Id.*

<sup>5</sup> *McNeal v. City of Waco*, 89 Tex. 83, 33 S.W. 322; *Stevenson v. Blake*, 131 Tex. 103, 113 S.W.2d 525

Sincerely,

*Daniell Davis*

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City of Houston Legal Department