

# **BUSINESS DAMAGES**

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## REPORTED CASES

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## BUSINESS DAMAGES

### I. INTRODUCTION

This paper analyzes damages that are recoverable in commercial and business cases. Rather than provide an exhaustive analysis of all commercial remedies, this paper covers damages commonly sought, including common law claims, statutory claims, as well as recovery of exemplary damages. Also discussed are appropriate pleading of damages, the evidence necessary to establish a right to recover those damages, and certain appellate issues regarding damages.

### II. BREACH OF CONTRACT

Commercial cases usually involve a breach of contract claim by one or more of the parties. There are various damage theories that parties can assert depending on the particular circumstances of their case.

The starting point in analyzing damages for breach of contract is to first understand the type of damages at issue. Texas law divides monetary damages for breach of contract into two main categories – direct and consequential. *Arthur Andersen & Co. v. Perry Equip. Corp.*, 945 S.W.2d 812, 816 (Tex. 1997).

#### A. Direct or General Damages

Direct or general damages are those damages that naturally and necessarily flow from a wrongful act and are therefore conclusively presumed to be a foreseeable consequence of a breach of contract or wrongful act. *Arthur Andersen*, 945 S.W.2d at 816. Thus, direct damages are imposed by law whether or not the parties contemplated the damages when they made the contract. *Id.*

Generally, direct damages may be measured in two ways: (1) the out-of-pocket loss; or (2) the benefit-of-the-bargain lost. *Miller v. Bynum*, 836 S.W.2d 160, 163 (Tex. 1992) (Phillips, C.J., concurring).

##### 1. Benefit of the Bargain

Texas law allows a party injured by a breach to sue for the benefit-of-the-bargain that the party would have received if the defendant had fully performed. *Arthur Andersen*, 945 S.W.2d at 817 (defining the out-of-pocket and benefit-of-the-bargain measures of recovery); *Miller*, 836 S.W.2d at 163. RESTATEMENT SECOND OF CONTRACTS § 347(a) (1981). The benefit of the bargain is measured by the difference of the value expected less the value received. *Arthur Andersen*, 945 S.W.2d at 817. Following are some contexts where this measure is used.

##### a. Service contracts

If a party contracts for services, the appropriate damages measure for breach generally is the reasonable cost of the expected performance. *P.G. Lake, Inc. v. Sheffield*, 438 S.W.2d 952, 956 (Tex. App.—Tyler 1969, writ ref'd n.r.e.).

##### i. construction contracts

In breach of contract cases based on construction contracts, damages are determined either by awarding (1) the difference in the value of the building as completed and the value of the building if completed in accordance with the plans and specification or (2) the cost of correction or completions. *See Turner, Collie, & Braden, Inc. v. Brookhollow, Inc.*, 642 S.W.2d 160, 164 (Tex. 1983); *A.B.C. Truck Rental and Leasing Co. v. Pletz*, 540 S.W.2d 532, 534 (Tex. Civ. App.-San Antonio 1976, writ ref'd n.r.e.). The means of computing damages in such cases is usually determined by whether the contract was substantially performed. *See Turner, Collie & Braden Inc.*, 642 S.W.2d at 164; *Chapa v. Reilly*, 733 S.W.2d 236, 237 (Tex. App.-Corpus Christi 1986, writ ref'd). If the contract was substantially performed, the damages will be computed under the remedial measure of damages method. *See Turner, Collie & Braden Inc.*, 642 S.W.2d at 164. However, if the contract was not substantially performed, the damages will be the "difference in value." *See Hutson v. Chambliss*, 157 Tex. 193, 300 S.W.2d 943 (1957). The "difference in value" approach is appropriate when the construction defects cannot be remedied without an expenditure disproportionate to the end to be attained and would result in economic waste. *Id.*

In an action for a breach of a service contract the unreasonableness of costs of repair is an affirmative defense. *P.G. Lake, Inc. v. Sheffield*, 438 S.W.2d 952, 956 (Tex. Civ. App.--Tyler 1969, writ ref'd n.r.e.) (holding that because the defendant failed to plead and prove the diminution in value to the plaintiff's land, the cost of repair damages awarded to plaintiff would be upheld despite the resulting economic waste).

##### ii. mitigation of damages

A defense available to a claim for damages in a service contract is the doctrine of mitigation of damages. For instance, an employee's damages for breach of an employment contract is reduced by any amount the plaintiff-employee earned or should, in the exercise of reasonable diligence, have earned through other employment. *Wal-Mart Stores, Inc. v. Amos*, 79 S.W.3d 178, 194 (Tex. App. – Texarkana 2002, no pet.). Likewise, a builder who is not allowed to finish the started work can recover the contract price less what would have been the cost to the builder of completing the work. *Vance v. My Apartment Steak*

*House of San Antonio, Inc.*, 677 S.W.2d 480, 482 (Tex. 1984).

Mitigation is an affirmative defense and the burden of pleading and proving facts showing it is on the claimant, as well as the burden of proving the amount the damages were increased by the failure to mitigate. *Rauscher Pierce Refsnes, Inc. v. Great Southwest Sav., F.A.*, 923 S.W.2d 112, 117 (Tex. App.—Houston [14th Dist.] 1996, no writ).

iii. mutual performance

Finally, a party to a contract may not enforce the contract or recover damages for its breach unless they have performed their obligations under the contract. *Carr v. Norstok Bldg. Sys., Inc.*, 767 S.W.2d 936, 941 (Tex. App.—Beaumont 1989, no writ). In some contexts, however, such as construction contracts, Texas courts apply the doctrine of substantial performance. *Vance*, 677 S.W.2d at 481.

b. Contracts for the sale of goods

The Uniform Commercial Code (“UCC”) governs damages recoverable upon breach of a contract for the sale of goods. TEX. BUS. & COM. CODE ANN. § 2.102 (Vernon 1994). “Where the U.C.C. applies, it displaces all common law rules of law regarding breach of contract and substitutes instead those rules of law and procedure set forth in the U.C.C.” *Glenn Thurman, Inc. v. Moore Constr., Inc.*, 942 S.W.2d 768, 771 (Tex. App.—Tyler 1997, no writ); *Bacchus Indus., Inc. v. Frontier Mech. Contractors*, 36 S.W.3d 579, 585 (Tex. App.—El Paso 2000, no pet.).

i. seller’s breach

When a seller of goods repudiates a contract, fails to make delivery, or delivers goods that may be justifiably rejected by the buyer, the buyer may recover the purchase price already paid, if any. TEX. BUS. & COM. CODE ANN. § 2.711(a). The UCC does not require that a buyer of nonconforming goods rework or re-fabricate the goods to make them conform to the original contract. *Aztec Corp. v. Tubular Steel, Inc.*, 758 S.W.2d 793, 800 (Tex. App.—Houston [14th Dist.] 1988, no writ). The buyer may also recover consequential and incidental damages. TEX. BUS. & COM. CODE ANN. § 2.714-715.

*Wilson v. Hays* provides a good example of the application of UCC principles. 544 S.W.2d 833, 834 (Tex. Civ. App.—Waco 1976, writ ref’d n.r.e.). There, the defendant contracted to sell the plaintiff 600,000 used bricks at a price of one cent per brick. *Id.* The plaintiff paid the defendant \$6,000 but the defendant delivered only 400,000 bricks. *Id.* The Tenth Court held that appropriate measure of damages under UCC sections 2.711 and 2.713 was the market price of the replacement brick (\$10,000), less the \$2,000 contract

price of the goods not received, equaling \$8,000. *Id.* at 836.

A buyer who elects not to cover a loss may recover the difference between the market value of the goods described in the contract and the contract price for those goods. TEX. BUS. & COM. CODE ANN. § 2.711(a)(1), 2.713. In the event that goods which do not satisfy the specifications in the contract are delivered and the buyer accepts the non-conforming goods, the buyer’s damages will be the difference between the goods as delivered and the value of the goods had they met the specifications of the contract. *Id.* § 2.714.

A non-breaching party need not show the market price of the goods if the non-breaching party elects its cover remedy. Where a buyer complies with the requirements of Texas UCC section 2.712, the buyer’s purchase price is presumed proper and the burden of proof is on the seller to demonstrate that the cover was not properly obtained. *Laredo Hides Co., Inc. v. H & H Meat Prod. Co., Inc.*, 513 S.W.2d 210, 221 (Tex. Civ. App.—Corpus Christi 1974, writ ref’d n.r.e.); *Mueller v. McGill*, 870 S.W.2d 673, 674 (Tex. App.—Houston [1st Dist.] 1994, writ denied) (holding that the plaintiff could cover by purchasing substitute goods, in good faith and without unreasonable delay or could elect to recover the difference between the contract price and the market price at the time he learned of the breach).

Where it is possible for a party to obtain cover at a price equal to or lower than that stated in the contract, the party has sustained no loss by the breach. *See Hickey v. Perkins Dry Goods Co.*, 229 S.W. 951, 954 (Tex. Civ. App.—Galveston 1921, no writ). The costs of cover are considered an item of general damages. *Hess Die Mold, Inc. v. American Plast-Plate Corp.*, 653 S.W.2d 927, 929 (Tex. App.—Tyler 1983, no writ). Allegations or findings that such damages were foreseeable to the breaching party are therefore not necessary, as general damages are deemed foreseeable. *Id.*

ii. buyer’s breach

Where a buyer breaches a contract to buy goods, the buyer is liable for the difference between the contract price and the market value of the goods or property at the time of the breach. TEX. BUS. & COM. CODE ANN. § 2.708(a). Should the difference in price fail to place the seller in as good a position as if the contract had been performed, the seller may recover profits that might have been made upon performance, together with incidental damages. TEX. BUS. & COM. CODE ANN. § 2.708(b); *Community Dev. Serv. v. Replacement Parts Mfg., Inc.*, 679 S.W.2d 721, 725 (Tex. App.—Houston [1st Dist.] 1984, no writ) (finding lost profits recoverable where evidence shows lost profits were a material and probable consequence of

breach and the breach and amount of damages are established with sufficient certainty).

When the difference between a contract price and a market price is a sufficient remedy, the market price is considered to be the price at which the goods were sold to a third party. TEX. BUS. & COM. CODE ANN. § 2.706. If the buyer has accepted the goods, thereby precluding a resale, the seller may bring an action for the contract price. *Id.* § 2.709.

## 2. Reliance Recovery

If the benefit of the bargain theory is inappropriate, then a party may recover reliance damages for breach of contract - those expenditures made in furtherance of the completion of contractual duties. Reliance damages are calculated by subtracting the value actually received under the contract, if any, from the value actually given or expended by the non-breaching party in reliance on the contract. *Arthur Andersen*, 945 S.W.2d at 817; RESTATEMENT (SECOND) OF CONTRACTS § 349. Reliance damages restore the non-breaching party to the same position as that party would have been in had the contract not existed. *Osage Oil & Ref Co. v. Lee Farm Oil Co.*, 230 S.W. 518, 519 (Tex. Civ. App.--Amarillo 1921, writ ref'd.) (finding, by implication, that the plaintiff could have engaged in business elsewhere during the frustrated performance tendered under the contract at issue); *see also Morgan v. Young*, 203 S.W.2d 837, 854 (Tex. Civ. App.— Beaumont 1947, writ ref'd. n.r.e.) (allowing farmer who attempted to mitigate damages by planting a crop subsequent to defendant's breach to recover expenses of mitigation where expenses were a reasonable sum, despite the fact farmer's loss was aggravated by his attempt to mitigate).

Reliance damages are well-suited for situations where the profit or gain to be derived from a bargain is uncertain. *See* RESTATEMENT (SECOND) OF CONTRACTS § 349 cmt. a (1981). Reliance damages also may adequately compensate a party where benefit-of-the-bargain damages are not easily proven to be foreseeable. *See id.* § 351(3). This measure of damages is particularly useful in the case of a new and unestablished business, where lost profits are difficult to prove with reasonable certainty.

Reliance damages are also sometimes claimed where the non-breaching party would suffer a loss under the contract. In this case, the defendant can prove as an offset the amount of the loss that the claimant would have suffered. *Mistletoe Exp. Service v. Locke*, 762 S.W.2d 637, 638 (Tex. App. – Texas 1988, no writ). Offset is an affirmative defense and must be pleaded and an amount proven within reasonable certainty. *Bonham State Bank v. Beadle*, 907 S.W.2d 465, 470, 38 Tex. Sup. Ct. J. 768 (Tex. 1995).

## 3. Quantum Meruit

Quantum meruit damages serve to return the plaintiff to a position as if no contract had been made. *Coon v. Schoeneman*, 476 S.W.2d 439, 441 (Tex. Civ. App.—Dallas 1972, writ ref'd n.r.e.). Based upon the premise that the other party has been unjustly enriched, quantum meruit recovery is appropriate where a contract is unenforceable, impossible, not fully performed, or void for other legal reasons. *R. Conrad Moore & Assocs., Inc. v. Lerma*, 946 S.W.2d 90, 97 (Tex. App.--El Paso 1997, writ denied). The right to recover in quantum meruit does not grow out of a written contract but instead out of a contract implied by law to prevent a party from receiving and knowingly accepting beneficial products or services without paying for the products or services provided. *Campbell v. Northwestern Nat'l Life, Ins. Co.*, 573 S.W.2d 496, 498 (Tex. 1978). The measure of damages in an action on quantum meruit is the reasonable value of the work performed and the materials furnished. *Thomason v. Freberg*, 588 S.W.2d 821, 830 (Tex. Civ. App.--Corpus Christi 1979, no writ).

Generally, a party may recover under quantum meruit only when there is no express contract covering the services on materials furnished. *Vortt Exploration Co. v. Chevron U.S.A., Inc.*, 787 S.W.2d 942, 944 (Tex. 1990); *Truly v. Austin*, 744 S.W.2d 934, 936 (Tex. 1988). Construction contracts are an exception to the general rule that quantum meruit recovery may not be obtained when there is an express contract covering the services or materials furnished. In such a case, a party may recover under either measure of damages. *See Murray v. Crest Constr., Inc.*, 900 S.W.2d 342, 345 (Tex. 1995) (per curiam) (holding where substantial performance is a condition precedent to recovery on an express contract, subcontractor could recover the amount of benefits conferred by its partial performance).

## B. Special or Consequential Damages

Special or consequential damages cover losses that follow naturally but not necessarily from the breach and are therefore recoverable only when the breaching party had notice or could have foreseen that the non-breaching party would suffer. *Arthur Andersen*, 945 S.W.2d at 817; *Mead v. Johnson Group, Inc.*, 615 S.W. 685, 687 (Tex. 1981). Following is a discussion of different types of special damages.

### 1. Lost Profits

#### a. Standard of recovery

Lost profits are recoverable as special damages if proven to be a natural, probable, and foreseeable

consequence of the defendant's breach.<sup>1</sup> *Kold-Serve Corp. v. Ward*, 736 S.W.2d 750, 755 (Tex. App.—Corpus Christi 1987, writ dismissed w.o.j.). *Narried v. Johnson*, 339 S.W.2d 566, 568 (Tex. Civ. App.—El Paso 1960, no writ) (finding that the plaintiff's inability to do business and resulting loss of profits were within the contemplation of the parties). The measure of such lost profits is “net” profits (what remains in the business after deducting from its total receipts all expenses incurred in carrying on the business), which must be shown by objective facts, figures, and data. *Turner v. PV Int'l Corp.*, 765 S.W.2d 455, 465 (Tex. App.—Dallas 1988, writ denied) (finding lost profits must be shown with “reasonable certainty”). As it is difficult to ascertain the exact amount of profits that would be earned in the future, it is not necessary to prove the amount of lost profits by precise calculation. *Szczepanik v. First S. Trust Co.*, 883 S.W.2d 648, 649 (Tex. 1994) (per curiam). There need be only sufficient data to establish lost profits with a reasonable degree of certainty. *Id.* This can be proven through testimony from a witness as to what profits would have been. *Naegeli Transp. v. Gulf Electroquip, Inc.*, 853 S.W.2d 737, 740 (Tex. App.—Houston [14th Dist.] 1993, writ denied). In proving lost profits, however, it is not always mandatory that testimony concerning lost profits be supplemented by the financial records from which the knowledge is gained if the person testifying has firsthand knowledge of the financial data. *Pena v. Ludwig*, 766 S.W.2d 298, 304 (Tex. App.—Waco 1989, no writ). Lost profits are not recoverable if they are dependent on uncertain or changing market conditions, chancy business opportunities, promotion of untested products or entry into unknown or unviable markets, or on the success of a new and unproven enterprise. *Texas Instruments, Inc. v. Teletron Energy Management, Inc.*, 877 S.W.2d 276, 279 (Tex. 1994).

The fact intensive determination incorporated in the reasonable certainty test for lost profits requires a showing of either the historic profitability of an activity, or the actual existence of contracts from which the amount of lost profits can be ascertained with a reasonable degree of certainty. *Associated Indem. Corp.*, 918 S.W.2d 580, 602 (Tex. App.—Corpus Christi 1990, no writ) *aff'd in part and rev'd in part on other grounds*, 964 S.W.2d 276 (Tex. 1998)). In addition, the Texas Supreme Court has approved of the introduction of verifiable future contracts in lieu of past profitability as a method of proving lost future profits. *Federal*

*Land Bank Ass'n. v. Sloane*, 825 S.W.2d 439, 442 (Tex. 1991).

Proof that a business operated at a loss, without more, is not evidence that will prove with reasonable certainty a claim for lost profits. *Turner*, 765 S.W.2d at 466. Similarly, testimony stating the amount of lost income, standing alone, is not sufficient to prove lost profits. *Holt Atherton Indus., Inc. v. Heine*, 835 S.W.2d 80, 83 (Tex. 1992).

A business established prior to the breach may submit evidence of its pre-existing profits, together with other facts and circumstances which indicate with reasonable certainty the amount of profits lost. *Southwest Battery Corp. v. Owen*, 115 S.W.2d 1097, 1098-99 (Tex. 1938). Profits can also be recovered for the normal increase in business which might have been expected in the light of past development and existing conditions. *Texas Instruments v. Teletron Energy Mgmt.*, 877 S.W.2d 276, 299 (Tex. 1994) (quoting *Southwest Battery Corp.*, 115 S.W.2d at 1098-99).

In *Wilson*, discussed at page 3, the court did not allow the plaintiff to recover consequential damages in the form of lost profits as there was no evidence that the plaintiff attempted to prevent or mitigate his loss. *Id.* “Consequential damages” includes any loss which could not reasonably be prevented by cover or otherwise. TEX. BUS. & COM. CODE ANN. § 2.715(b). The burden of proof regarding consequential damages is on the plaintiff, and there was no evidence introduced to support a jury award of consequential damages. *Wilson*, 544 S.W.2d at 836.

In *Szczepanik*, 883 S.W.2d 648, 650 (Tex. 1994), the Texas Supreme Court found legally insufficient evidence of lost profits because there was no established link which related the total amount of expected profits to the amount of profits they allegedly lost. Acknowledging that lost profits need not be proven by exact calculation, the court reasoned that “the injured party must do more than show that they suffered some lost profits.” *Id.* at 649. The evidence must establish the amount of lost profits with reasonable certainty. *Id.* What constitutes reasonable certain evidence of lost profits is a fact-intensive determination to be determined on a case-by-case basis. *Id.* At a minimum, opinions or estimates of lost profits must be based on objective facts, figures, or data from which the amount of lost profits may be ascertained. *Id.* See also *Holt Atherton Indus., Inc. v. Heine*, 835 S.W.2d, 80, 84 n.5 (Tex. 1992).

In *Texas Instruments*, an engineer hired Texas Instruments to develop the prototype of a product for which there was no comparable device in existence or on the market. *Id.* After two years of unsuccessful attempts to develop a working prototype, Texas Instruments ceased development. *Id.* The plaintiff sued Texas Instruments for breach of contract, breach of

<sup>1</sup> If a trial court submits a jury question on lost profits, it must also submit a question on the foreseeability of the lost profits. See *Winkle Chevy-Olds Pontiac v. Condon*, 830 S.W.2d 740, 746-47 (Tex. App. — Corpus Christi 1992, writ dismissed).

warranty, and DTPA violations. *Id.* The jury awarded lost profits. *Id.*

The Texas Supreme Court reversed and rendered judgment on the award for lost profits, explaining that although the fact that a business is new is “but one consideration” in determining whether lost profits have been proven with reasonable certainty, the mere hope that an untried enterprise will be successful, even if it is a realistic one, will not support a recovery of lost profits. *Id.* at 280. Citing two of its prior decisions, the court pointed out that the focus must be the experience of the persons involved in the new enterprise, the nature of the business activity, and the relevant market. *Id.* at 279-80. *cf. Southwest Battery Corp. v. Owen*, 131 Tex. 423, 115 S.W.2d 1097 (1938) (affirming award of lost profits although venture was new where a well-established market existed for the product and evidence of a brief sales history). *Pace Corp. v. Jackson*, 155 Tex. 179, 284 S.W.2d 340 (1955) (affirming award of lost profits where new business had operated at a profit prior to the breach of contract, and the business owner had considerable experience in and knowledge of the industry); *Aboud v. Schlichtemeier*, 6 S.W.3d 742 (Tex. App.—Corpus Christi 1999, pet. denied) (upholding lost profits damage award where partners had well established track record of success in similar ventures).

#### b. Proof of net profits

Lost profits must be based on net profits, not gross revenues. *Holt Atherton Indus., Inc. v. Heine*, 835 S.W.2d 80, 83 n.1 (Tex. 1992). “Net Profits” is defined as the difference between a business’s total receipts and all of the expenses incurred in carrying on the business. *Texaco, Inc. v. Ngyen*, 137 S.W.3d 763 (Tex. App. – Houston [1st Dist.] 2004, no pet. h.). Several Texas courts have held that evidence of expected profit margin, shown by deducting operating expenses, is a reasonable basis for calculating net profits. *See, e.g., White v. Southwestern Bell Tel. Co.*, 651 S.W.2d 260, 262-63 (Tex. 1983); *Travel Masters, Inc. v. Star Tours, Inc.*, 830 S.W.2d 614, 620-21 (Tex. App. – Dallas 1992) *rev’d on other grounds*, 827 S.W.2d 830 (Tex. 1992); *Keller v. Davis*, 694 S.W.2d 355, 357 (Tex. App. – Houston [14th Dist.] 1985, writ ref’d n.r.e.).

*Holt Atherton* illustrates legal sufficiency problems that can arise when attempting to prove lost profits. That case involved the failure of Holt Machinery Company to pay for the repairs to the plaintiff’s bulldozer based on an oral warranty. *Id.* at 82. The plaintiffs claimed they sustained lost profits over a thirteen month period due to loss of use of the bulldozer. *Id.* at 84-85. During the relevant period, the plaintiffs had two bulldozers that operated about half of the time because business was slow. *Id.* at 85. Based on this testimony, the court stated that the plaintiffs failed to prove that there was enough work to keep two

bulldozers working full-time during the period that the defendant had retained possession of the bulldozer and that they were entitled to recover lost profits for the entire thirteen month period. *Id.* According to one of the plaintiff’s testimony, defendant only kept the bulldozer for eight months before starting repairs. *Id.* Although the plaintiffs testified that they lost several contracts because they did not have the bulldozer available, they were not able to specify which contracts they lost, how many they lost, or how much profit they would have had from the contracts or who would have awarded them contracts. *Id.* Thus, the supreme court held the evidence was legally insufficient to support the award.

*Formosa* also illustrates when the underlying evidence supporting an award for lost profits is too speculative to recover. There, Presidio sued Formosa for fraudulently inducing it to enter into a construction contract. *Id.* at 43. The jury found that Formosa had defrauded Presidio, enticing it to make a low bid on the proposed construction project by misrepresenting in the bid package the scheduling, delivery of material, and responsibility for delay damages. *Id.* at 44. The trial court suggested a remittitur, in lieu of the damages awarded by the jury, to \$700,000 for tort damages and \$467,000 for contract damages. *Id.* Presidio elected the tort damages, thus accepting the trial court’s remittitur for \$700,000 in actual damages and \$10 million in punitive damages. *Id.* The Supreme Court sustained the liability finding, thus holding that Presidio was entitled to recover the difference between the anticipated value of the contract and the actual value it received (i.e., “benefit-of-the bargain” damages) — which included Presidio’s expected profit margin. *Id.* at 49-50.

However, the court found no support for the entire amount of the “benefit-of-the-bargain” damages that the jury awarded despite specific testimony from Presidio’s president on how it would have bid had no misrepresentations been made by Formosa, and on what its profit would have been. *Id.* at 50-51. Given the fact that Presidio calculated its damages claim on the premise that it would have been awarded the contract by bidding the project at an amount which Formosa had in fact rejected, the court noted that “while a benefit-of-the-bargain measure can include lost profits, it only compensates for the profits that would have been made if the bargain had been performed as promised.[The] doubling of Presidio’s bid is entirely speculative because there is no evidence that Presidio would have been awarded the project if it had made a \$1.3 million bid.” *Id.* at 50. Having found Presidio’s evidence as to its damages (including lost profits) inadequate to sustain the trial court’s remittitur, the supreme court reversed the award for damages and remanded the case for new trial. *Id.* at 52.

### C. House Bill 4

The Texas Legislature, recently enacted House Bill 4. See Act approved June 11, 2003, 78th Leg., R.S., RB. 4 § 13.04 the amended Texas Civil Practices and Remedies Code now requires claimants to prove their loss of earnings or earning capacity net of any federal income tax payment or liability. *Id.* Courts are also directed to instruct juries as to whether any of the claimants' recovery of compensatory damages is subject to state or federal income taxes. *Id.* § 13.09.

### D. Cases Upholding Recovery for Lost Profits

Generally stated, plaintiffs who have successfully recovered lost profits have done so in one of two ways: through the use of either (1) comparisons to past periods of profit or similar enterprises, whether their own or others; or (2) financial experts who have presented articulate and well-founded damage models that include verifiable mathematical calculations and identification of lost contracts. The following are cases where the court has upheld lost profit awards.

- *DSC Communications v. Next Level Communications*, 107 F.3d 322, 329 (5th Cir. 1997) (affirming award of future lost profits where plaintiff's damage expert presented a damage model that included assumption of future market share based his assumption on data obtained from respected sources in the telecommunications market and upon a showing that plaintiff's history of strong performance in the field was indicative of likely success). *Id.* at 329.
- *Helena Chem. Co. v. Wilkins*, 47 S.W.3d 46, 504-06 (Tex. 2001) (holding evidence was legally sufficient to support the jury's damage award for lost profits where there was testimony regarding the market value of lost crops based on the United States Agricultural Stabilization Conservation Services farm-shield data and testimony regarding transportation costs, grain elevator drying costs, lease expenses, and the actual price of the seed).
- *White v. Southwestern Bell Tel. Co., Inc.*, 651 S.W.2d 260 (Tex. 1983) (reversing trial court's directed verdict on lost profits where the plaintiff used preexisting profits from his 33-year old flower business.).
- *Carter v. Steverson & Co.*, 106 S.W.3d 161 (Tex. App.—Houston [1st Dist.] 2003, pet. denied) (affirming award of lost profits where the jury had before it both favorable and unfavorable evidence substantiating the plaintiff's claims to lost profits).
- *Munters Corp. v. Swissco-Young Indus., Inc.*, 100 S.W.3d 292, 300-02 (Tex. App.—Houston [1st Dist.] 2002, no pet.), (affirming award of lost profits where evidence showed company had been profitable and with evidence that calculated lost profits by discounting its estimated cash inflows and liquidation value).
- *Goose Creek Consol. Indep. Sch. Dist. v. Jarrar's Plumbing, Inc.*, 74 S.W.3d 485, 491 (Tex. App.—Texarkana 2002, pet. denied) (upholding a jury award for loss of value where the claimant provided a formulation that calculated the diminution of value).
- *Foust v. Estate of Rollins*, 21 S.W.3d 495, 504-06 (Tex. App.—San Antonio 2002, pet. denied) (affirming a jury award for lost profits for lost crops where plaintiff presented evidence which took into account the expenses of cultivating and bringing the crops to market).
- *Two Thirty-Nine Joint Venture v. Joe*, 60 S.W.3d 896, 911 (Tex. App.—Dallas 2001, pet. denied) (holding that evidence of lost profits was sufficient to raise a fact issue where plaintiffs presented expert affidavit that the loss of the real estate sale cost was \$119,770 in carrying costs and that a reasonable value in investing the proceeds from the sale would have produced a rate of return calculated by the rates of return on an average investment of another real estate opportunity.)
- *Vingcard v. Merrimac Hospitality Sys., Inc.*, 59 S.W.3d 847, 862-65 (Tex. App.—Fort Worth 2001, pet. denied) (affirming a jury award for lost profits where the plaintiff submitted evidence regarding the projected sales of two computer units via its expert witness who based his calculations on the facts, figures, and data and his many years of experience in the touch-screen based computer industry.)
- *Abraxas Petroleum Corp. v. Hornburg*, 20 S.W.3d 741, 760-61 (Tex. App.—El Paso 2000, no pet.) (affirming jury award of lost profits where plaintiff's expert projected a future income stream based on a predicable decline curve of the production of the oil and gas reservoir, and proved the market value of a working interest by subtracting the projected lease operating expenses from the projected future income stream as applied to the facts of the case).
- *Interceramic, Inc. v. South Orient R.R., Co., Ltd.*, 999 S.W.2d 920, 928 (Tex. App.—Texarkana 1999, pet. denied) (affirming bench finding of lost profits where lost profits were based on objective facts and data based on the expert testimony and the corroborating testimony of plaintiff's chief operating officer).
- *Anthony Equip. Corp. v. Irwin Steel Elevators*, 115 S.W.3d 191, 204-05 (Tex. App. — Dallas 2003, pet. dismissed) (affirming award of lost profits where claimant offered evidence that he lost a

contract due to defendant's breach of contract and evidence of the profit it would have made had the lost contract not been cancelled)

### E. Cases Disallowing or Reducing Recovery of Lost Profits

The following cases are where the court held lost profits were unrecoverable.

- *Burkhart Grob Luft und Raumfahrt GmbH & Co. KG v. E-Systems, Inc.*, 257 F.3d 461, 467-68 (5th Cir. 2001) (affirming the district court's decision not to submit the issue of the plaintiff's lost profits to the jury where there was no evidence that plaintiff would have been the winner in the bidding contest for the contract).
- *Great Pines Water Co., Inc. v. Liqui-Vox Corp.*, 203 F.3d 920, 922-24 (5th Cir. 2000) (disregarding jury determinations regarding lost profits where claimant did not produce any definitive evidence such as contemporary business records, service cancellation slips, relevant computer entries, or customer complaint list on the central issue of how many customers had cancelled due to the problems with the product).
- *Information Communication Corp. v. Unisys Corp.*, 181 F.3d 629, 633 (5th Cir. 1999) (affirming a take-nothing judgment which had precluded a finding of lost profits that a "paradigmatic new and unproven business" and had no track record of successfully creating and marketing new products).
- *Dyll v. Adam*, 167 F.3d 945, 946-48 (5th Cir. 1999,) (holding that the evidence submitted by the plaintiff was insufficient to establish that the technology would have earned a profit with reasonable certainty).
- *Miga v. Jensen*, 96 S.W.3d 207 (Tex. 2002) (holding that the evidence was legally insufficient to show that plaintiff suffered reasonably certain business losses resulting from defendant's breach).
- *United Mobile Networks, L.P. v. Deaton*, 939 S.W.2d 146 (Tex. 1997) (reversing award of conversion damages where claimant failed to show which customers were lost due to conversion of customer list).
- *Holt Atherton Indus., Inc. v. Heine*, 835 S.W.2d 80, 85 (Tex. 1992) (reversing award of lost profits where claimant failed to show he had enough work to occupy full-time work for bulldozer).
- *Aquila Southwest Pipeline, Inc. v. Harmony Exploration, Inc.*, 48 S.W.3d 225, 245-46 (Tex. App.—San Antonio 2001, no pet.) (affirming the trial court's finding that there was insufficient evidence to support the jury's award on lost

profits where expert's methodology while sound, was supported by speculative facts).

- *Haynes & Boone v. Bouldin, Ltd.*, 896 S.W.2d 179, 182-83 (Tex. 1995) (reversing award of damages for lost of investment due to foreclosure in malpractice action against lawyer where there was no evidence that the alleged malpractice was the result of the foreclosure on the leased premises).
- *Texaco, Inc. v. Nguyen*, 137 S.W.3d 763 (Tex. App. — Houston [1st Dist. 2004, no pet. h.) (reversing award of lost profits where claimants failed to provide a complete calculation of net profits).
- *Edmunds v. Sanders*, 2 S.W.3d 697, 705-06 (Tex. App.—El Paso 1999, pet. denied) (finding legally insufficient evidence to support award of lost profits when plaintiff's evidence was not based on a calculation of net profits, but instead was based on an average percentage of profits for similar businesses as shown in certain trade manuals).
- *Capital Metro. Trans. Auth. V. Central of Tx. Railway and Navigation Co., Inc.*, 114 S.W.3d 573, 581-82 (Tex. App. — Austin 2003, pet. denied) (reversing jury award of lost profits where claimant's expert acknowledged that the business lost money every year that the claimant had operated the rail line, there were no contracts to support his opinion that revenue would increase, and testimony about the future amount of work that the company would perform was based on unfounded assumptions).

To conclude, courts will look to various factors to determine if lost profits are recoverable in a particular case, including the experience of the principals, establishment of the industry, the novelty of the product or enterprise, whether the enterprise is ongoing or new, and the past profitability of the business or like businesses. No single element will allow or prohibit recovery of lost profits. Instead, as noted above, entitlement to lost profits is a fact intensive inquiry.

#### 1. Mental Anguish

A party cannot normally recover mental anguish damages in a breach of contract action or a tort based upon a right growing out of a breach of contract. These damages are seen as difficult to predict and verify. *City of Tyler v. Likes*, 962 S.W.2d 489, 494 (Tex. 1997); *see also Rogowicz v. Taylor & Gray, Inc.*, 498 S.W.2d 352, 355-56 (Tex. Civ. App.—Tyler 1973, writ ref'd. n.r.e.). *See Rubalcaba v. Pacific/Atlantic Crop Exch., Inc.*, 952 S.W.2d 552, 558 (Tex. App.—El Paso 1997, no writ).

Plaintiffs can recover mental anguish damages in the rare instance that the nature of the contract is such

that mental anguish is a natural result of a breach. These situations usually involve personal services or a high degree of mental suffering. *See, e.g., Pat H. Foley & Co. v. Wyatt*, 442 S.W.2d 904, 907 (Tex. Civ. App.—Houston [14th Dist.] 1969, writ ref'd n.r.e.) (upholding award of mental anguish damages against funeral home for mistreatment of corpse); *City of Dallas v. Brown*, 150 S.W.2d 129, 131 (Tex. Civ. App.—Dallas 1941, writ dismissed w.o.j.) (allowing mental damages in case where termination of widow's water service was clearly wrongful and nature of contract rendered mental anguish damages foreseeable). *But see Temple-Inland Forest Prod. Corp. v. Carter*, 993 S.W.2d 88, 93 (Tex. 1999) (refusing to permit mental anguish damages resulting from an increased possibility of asbestos related disease); *Pat H. Foley & Co.*, 442 S.W.2d at 907 (finding mother's mental concern, sensibilities, and solicitude to be the prime considerations of her contract with funeral home hired to inter her son's body).

## 2. Liquidated Damages

Some contracts provide a set amount of damages, called liquidated damages, written into the contract in lieu of the remedies that the law provides. *Murphy v. Cintas Corp.*, 923 S.W.2d 663, 666 (Tex. App.—Tyler 1996, pet. denied). Liquidated damages clauses are common in contracts for sale of real estate where the contract provides for a forfeiture of earnest money and in construction contracts where there is unexcused delay. A party claiming liquidated damages must prove that the harm caused by the breach is incapable or difficult of estimation that the amount of liquidated damages called for is a reasonable estimate of just compensation. *Baker v. International Record Syndicate*, 812 S.W.2d 53, 55 (Tex. App.—Dallas 1991, no writ) (upholding liquidated damages clause in photographer's contract with company because the actual value of the photos would have been difficult to determine). Otherwise, the clause is considered as an unenforceable penalty. *Phillips v. Phillips*, 820 S.W.2d 785, 788 (Tex. 1992) (holding that liquidated damages clause unenforceable where damages not incapable of estimation and because clause required actual damages be multiplied by ten).

A party does not waive the penalty defense by not pleading it if a penalty is apparent on the face of the petition and established as a matter of law. *Phillips*, 820 S.W.2d at 788. Once pleaded, that party bears the burden to conclusively establish that the clause is unenforceable as a matter of law. *Baker v. Int. Record Syndicate, Inc.*, 812 S.W.2d 530 (Tex. App.—Dallas 1991, no writ). Because the issue of penalty is decided as a matter of law, counsel can preserve error by moving for summary judgment, moving for a directed verdict, and by moving for a judgment notwithstanding

the verdict. TEX. R. CIV. P. 301; *Fort Worth State School v. Jones*, 756 S.W.2d 445, 446 (Tex. App.—Fort Worth 1988, no writ).

## 3. Nominal Damages

Even where a plaintiff fails to prove actual damages, he still may be entitled to recover nominal damages, those that are damages in name only and are small or even trivial in amount. *Hutchinson v. Texas Aluminum Co.*, 330 S.W.2d 895, 898 (Tex. Civ. App.—Dallas 1971, writ ref'd n.r.e.); *Lucas v. Morrison*, 286 S.W.2d 190, 191-92 (Tex. Civ. App.—San Antonio 1956, no writ). Nominal damages also may be recoverable where a plaintiff proves only collateral losses that were not within the contemplation of the parties at the time of contracting. *McGuire v. Osage Oil Corp.*, 55 S.W.2d 535, 537 (Tex. Comm'n App. 1932, holding approved). Nominal damages may not be awarded. Where the defendant negates the existence of damages. *Gulf Coast Inv. Corp. v. Rothman*, 506 S.W.2d 856, 858 (Tex. 1974) (finding that where plaintiff failed to prove damages and defendant introduced evidence that plaintiff suffered no loss, an award of even nominal damages was improper).

Although trivial in amount, nominal damages can support an award of costs. *Arnold v. Tarrant Beverage Co.*, 215 S.W.2d 894, 895-96 (Tex. Civ. App.—Galveston 1948, writ ref'd n.r.e.).

## 4. Exemplary Damages

Exemplary damages are generally not recoverable in contract actions. *Amoco Prod. Co. v. Alexander*, 622 S.W.2d 563, 571 (Tex. 1981). Even if a breach of contract is malicious, intentional or capricious, exemplary damages may not be recovered unless a distinct tort theory is alleged and proved. *Id.* Neither gross negligence in a breach of contract nor gross negligence in the inducement to contract will entitle a non-breaching party to exemplary damages. *D.S.A., Inc. v. Hillsboro Indep. Sch. Dist.*, 973 S.W.2d 662, 664 (Tex. 1998) (per curiam) (negligent misrepresentation); *Jim Walter Homes, Inc. v. Reed*, 711 S.W.2d 617, 618 (Tex. 1986) (breach of contract).

Contractual relationships may create duties under both contract and tort law. *See Jim Walter Homes*, 711 S.W.2d at 618. "The acts of a party may breach duties in tort or contract alone or simultaneously in both. The nature of the injury most often determines which duty or duties are breached. When the injury is only the economic loss to the subject of a contract itself, the action sounds in contract alone." *Id.*; *see also Formosa Plastics*, 960 S.W.2d at 46-47.

Even if an award of punitive damages is allowable in a given case, the award must still pass constitutional muster. Last year, the United States Supreme Court reversed a Utah state court award of \$145 million in punitive damages. *State Farm Mut. Auto Ins. Co. v.*

*Campbell*, — U.S. —, 123 S. Ct. 1513, 1526 (2003). In reversing the award, the Court outlined the principles set forth in its own previous precedent, *BMW of North America, Inc. v. Gore*, 517 U.S. 559 (1996). 123 S. Ct. at *passim*. In applying *Gore*, the *State Farm* Court held that the \$145 million award in punitive damages violated the Due Process Clause of the United States Constitution for several reasons. First, the award constituted a punishment for, among other things, acts that were committed outside of Utah, and which may have been lawful in other jurisdictions. *Id.* at 1521-24. Second, because the award of actual compensatory damages was only \$1 million, the ratio between the punishment and the actual harm was 145 to 1, a presumptively excessive award for constitutional purposes. *Id.* at 1524 (“[F]ew awards exceeding a single-digit ratio between punitive and compensatory damages, to a significant degree, will satisfy due process.”). Finally, the most relevant civil sanction under Utah law for the reprehensible conduct was \$10,000; accordingly, the Court held that the \$145 million punitive award was a constitutionally disparate civil punishment. *Id.* at 1526.

#### 5. Attorney’s Fees

Texas law does not allow for the recovery of attorney’s fees in the absence of a contract provision or statute. *New Amsterdam Cas. Co. v. Texas Indus., Inc.*, 414 S.W.2d 914, 915 (Tex. 1967). The Texas Civil Practice and Remedies Code allows recovery of attorney’s fees in an action for breach of an oral or written contract. TEX. CIV. PRAC. & REM. CODE ANN. § 38.018 (Vernon 1997). A party claiming attorney fees must prove that he is represented by an attorney, that he has presented his claim for attorney’s fees to the opposing party, and that the opposing party failed to pay the claim within thirty days of the presentment. *Id.* § 38.002.

Numerous other statutes, such as the Texas Insurance Code and the Deceptive Trade Practices Act, allow for recovery of attorneys fees.

### F. Pleading Damages

#### 1. Direct Damages

Alleging of a breach of contract or other wrongdoing is generally sufficient notice of general damages. *Sherrod v. Bailey*, 580 S.W.2d 24, 28 (Tex. Civ. App.—Houston [1st Dist.] 1979, writ ref’d n.r.e.); *Khalaf v. Williams*, 814 S.W.2d 854, 858 (Tex. App.—Houston [1st Dist.] 1991, no writ)

#### 2. Consequential Damages

Consequential damages should be pleaded to set out the particular loss and how it was both contemplated and caused by the breach because they vary with the circumstances of each case. TEX. R. CIV. P. 56; *Sherrod*, 580 S.W.2d at 28. Defendants should

specially except to a general prayer for damages and timely assert objections at trial to the admission of special damage evidence that the plaintiff has not specifically pleaded or the issue may be tried by consent. TEX. R. CIV. P. 67; *Sage St. Assoc. v. Northdale Const.*, 863 S.W.2d 438, 445 (Tex. 1993), *rev’d on other grounds*, 937 S.W.2d 425 (Tex. 1996). Being specific will protect the party from defending a waiver claim in the event they recover these damages. *See Burke v. Union Pac. Res. Co.*, 138 S.W.2d 46 (Tex. App. – Texarkana 2004, Rule 53 Motion filed).

### G. Proving Damages

#### 1. Cause in Fact of Damages

To recover damages for breach of contract, a claimant must prove that his damages would not have occurred “but for” the other party’s breach and that the damages are a natural, probable, and foreseeable consequence of the defendant’s conduct. *Mead v. Johnson Group, Inc.*, 615 S.W.2d 685, 687 (Tex. 1981); *Nelson Cash Register v. Data Terminal Sys., Inc.*, 671 S.W.2d 594 (Tex. App.—San Antonio 1984, no writ) (holding that there was insufficient evidence that the breaches found by the jury caused the damage to plaintiff’s business); *see also Prudential Sec., Inc. v. Haugland*, 973 S.W.2d 394, 395-96 (Tex. App.—El Paso 1998, pet. denied).

#### 2. Foreseeability of Damages

A claimant must also prove that the injury stemming from the contract breach foreseeable - a natural and probable consequence of the defendant’s conduct and also was within the contemplation at the time they made the parties’ contract. *Hadley v. Baxendale*, is often cited as the seminal case on foreseeability of contract damages:

Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.

9 Exch. 341, 354 (1854).

A majority of American jurisdictions have adopted the Hadley Rule. RESTATEMENT OF CONTRACTS § 365 (1981).

Damages that are not directly traceable to the wrongful act or are not foreseeable cannot be recovered. *Stuart v. Bayless*, 964 S.W.2d 920, 921-22 (Tex. 1998) (holding that loss of potential contingency fees by law firm not foreseeable at the time the contract was made by law firm and client who failed to pay attorney fees).

The jury charge should include an instruction on foreseeability. TEX. R. CIV. P. 278. Although trial courts tend to submit foreseeability in terms of proximate cause, courts of appeals have criticized this practice. (Tex. Civ. App.—Houston [1st Dist.] 1979, writ ref'd n.r.e.). See, e.g., *Prudential Securities, Inc. v. Haughland*, 973 S.W.2d 394, 397 n.2 (Tex. App. — El Paso 1998, pet. denied); *Winograd v. Clear Lake City Water Auth.*, 811 S.W.2d 147, 156 (Tex. App. — Houston [1st Dist.] 1991, writ denied). Thus, counsel should consider objecting to the failure to require that damages be foreseeable in the charge to preserve any error.

### 3. Certainty of Amount of Damages

In addition to proving cause in fact and foreseeability, plaintiffs must prove contract damages with sufficient certainty to allow a trier of fact to compute the appropriate amount to award. The certainty standard does not require proof of damages with mathematical certainty, but only within reasonable certainty. *Wilfin, Inc. v. Williams*, 615 S.W.2d 242, 244 (Tex. Civ. App.—Dallas 1981, writ ref'd n.r.e.) (holding general contractors' uncontroverted testimony that landscaping business usually received one-third of the bid as a profit sufficient to support an \$8,000 award where the bid was \$25,090).

Conversely, a party cannot recover damages that are speculative and cannot be determined with reasonable certainty. *Southwest Battery Corp. v. Owen*, 115 S.W.2d 1097, 1099 (Tex. 1938). Nonetheless, a party who breaches a contract cannot escape liability merely because it is impossible for the plaintiff to prove a perfect measure of damages. *Id.* at 1099. The determination as to what constitutes reasonable certainty depends on the facts and circumstances of each case. *Texas Instruments, Inc. v. Teletron Energy Mgmt., Inc.* 877 S.W.2d 276 (Tex. 1994).

### 4. Contorts

Before *Formosa Plastics*, Texas courts generally did not allow parties to recover tort damages in a case involving an alleged breach of contract unless the plaintiff suffered an injury that was distinct, separate and independent from the economic losses recoverable under the breach of contract claim. See, e.g., *Grace Petroleum Corp. v. Williamson*, 906 S.W.2d 66, 68-69 (Tex. App.—Tyler 1995, no writ); *Barbouti v. Munden*, 866 S.W.2d 288, 293-94 (Tex. App.—

Houston [14th Dist.] 1993, writ denied); *C&C Partners v. Sun Exploration & Prod. Co.*, 783 S.W.2d 707, 719-20 (Tex. App.—Dallas 1989, writ denied). These cases based their decisions on two Texas Supreme Court opinions. See *Southwestern Bell Tel. Co. v. DeLanney*, 809 S.W.2d 493 (Tex. 1991); *Jim Walter Homes, Inc. v. Reed*, 711 S.W.2d 617 (Tex. 1986) (holding that when the plaintiff's injury is nothing more than the economic loss of a contract, the action sounds in contract alone and tort damages are not recoverable); see also *Miga v. Jensen*, 96 S.W.3d 207, 211 (Tex. 2002) (finding the mere fact that there is a dispute between the parties regarding the terms of an agreement does not transform a contractual disagreement into a fraud claim).

*Formosa Plastics* clarified this rule when it held that parties do have a legal duty not to fraudulently procure a contract that is separate and independent from the duties established by the contract itself. *Formosa Plastics*, 960 S.W.2d at 46-47.

Because the *Formosa Plastics* decision is limited to fraudulent inducement cases it probably does not affect prior case law addressing the circumstance where a person is seeking recovery for fraud associated with the alleged breach of contract to avoid the statute of frauds or to make a back door for recovery of punitive damages. See, e.g., *J. Parra e Hijos, S.A. de C. V. p. Barroso*, 960 S.W.2d 161, 169 (Tex. App.—Corpus Christi 1997, no pet.) (exemplary damages); *Leach*, 892 S.W.2d at 960-61 (statute of frauds); *Peco Constr. Co. v. Guajardo*, 919 S.W.2d 736, 739 (Tex. App.—San Antonio 1996, writ denied). In these cases, benefit-of-the-bargain damages will probably still be unavailable on the fraud claim. See, e.g., *Facciolla p. Linbeck Constr. Corp.*, 968 S.W.2d 435, 448-49 (Tex. App.—Texarkana 1998, no pet); *Leach v. Conoco, Inc.*, 892 S.W.2d 954, 960-61 (Tex. App.—Houston [1st Dist.] 1995, writ dismissed w.o.j.); *Gold Kist, Inc. v. Carr*, 886 S.W.2d 425, 431-32 (Tex. App.—Eastland 1994, writ denied); *Collins v. McCombs*, 511 S.W.2d 745, 747 (Tex. Civ. App.—San Antonio 1974, writ ref'd n.r.e.).

A party alleging an independent tort in addition to the contract duties must plead and prove the tort in addition to the breach of contract. *Crawford v. Ace Sign, Inc.*, 917 S.W.2d 12, 14 (Tex. 1996) (per curiam) (holding that absent proof that defendant's conduct would give rise to liability outside the contract, the action sounds in contract); *Southwestern Bell Tel. Co. v. DeLanney*, 809 S.W.2d 493, 494-95 (Tex. 1991) (finding that action was in contract and not in tort, because plaintiff's claims against telephone company for failure to publish yellow pages advertisement arose solely from the contract, and the damages were only for economic loss); *Texas Power & Light Co. v. Barnhill*, 639 S.W.2d 331, 334 (Tex. App.—Texarkana 1982, writ ref'd n.r.e.) (denying exemplary damages

where evidence was factually insufficient to prove independent tort). *But see Formosa Plastics*, 960 S.W.2d at 47 (noting that recovery of exemplary damages is allowable where fraud in the inducement of a contract is properly pleaded and proven, because a fraud action is not based solely upon the contract).

The tort and the breach of contract need not arise out of separate and distinct transactions. *Formosa Plastics*, 960 S.W.2d at 47; *Texas Power*, 639 S.W.2d at 334. Some contracts also involve special relationships that give rise to a duty enforceable as a tort. *See, e.g., Sanus/New York Life Health Plan, Inc. v. Dube-Seybold-Sutherland Mgmt. Inc.*, 837 S.W.2d 191, 199 (Tex. App.—Houston [1st Dist.] 1992, no writ) (“When special confidence is placed in one who thereby obtains a resulting superiority of position and influence, a special relationship is created.”). A party injured by a duty arising from a special relationship may be entitled to exemplary damages as a result of a breach of the fiduciary duty. *Id.* at 200; *see also Manges v. Guerra*, 673 S.W.2d 180, 184 (Tex. 1984) (holding that where suit is based on breach of fiduciary duty, and not on breach of contract, exemplary damages may be recovered).

##### 5. The Economic Loss Rule

One principle derived from the separation of contract and tort law is the economic loss rule. This rule provides that where a product injures a party economically and not physically, the party may recover those damages only under the warranties provided by the Uniform Commercial Code but not under tort theories. *Nobility Homes of Texas, Inc. v. Shivers*, 557 S.W.2d 77, 79 (Tex. 1977). The economic loss rule applies to negligence and strict liability claims. *Mid Continent Aircraft Corp. v. Curry County Spring Serv., Inc.*, 572 S.W.2d 308, 312-13 (Tex. 1978); *Indelco, Inc. v. Hanson Indus. N. America-Grove Worldwide*, 967 S.W.2d 931, 932-33 (Tex. App.—Houston [14th Dist.] 1998, pet. denied) (economic losses caused by defective product damaging itself are not recoverable through a suit alleging negligence); *Equistar Chemicals, L.P. v. Dresser-Rand Co.*, 123 S.W.3d 584 (Tex. App. [14th Dist.] 2003, pet. filed).

In *Nobility Homes*, the Texas Supreme Court defined economic loss as both direct and indirect:

Direct economic loss may be said to encompass damage based on insufficient product value; thus, direct economic loss may be “out of pocket” – the difference in value between what is given and received – or “loss of bargain” – the difference between the value of what is received and its value as represented. Direct economic loss may also be measured by cost of replacement and repair. Consequential economic loss

includes all indirect loss, such as loss of profits resulting from inability to make use of the defective product.

*Nobility Homes*, 557 S.W.2d at 78, n.1.

The Texas Supreme Court later explained the rationale for applying contract law to economic losses:

Distinguished from personal injury and injury to other property, damage to the product itself is essentially a loss to the purchaser of the benefit of the bargain with the seller. Loss of use and cost of repair of the product are the only expenses suffered by the purchaser. The loss is limited to what was involved in the transaction with the seller, which perhaps accounts for the legislature providing that parties may rely on sales and contract law for compensation of economic loss to the product itself.

*Mid Continent Aircraft Corp. v. Curry County Spring Serv., Inc.*, 572 S.W.2d 308, 312-13 (Tex. 1978); *see also Hininger v. Case Corp.*, 23 F.3d 124, 127 (5th Cir. 1994) (precluding economic losses as lost profits based on negligence theory in suit against component supplier), *cert. denied*, 513 U.S. 1079 (1995); *Coffey v. Fort Wayne Pools, Inc.*, 24 F. Supp. 2d 671, 687 (N.D. Tex. 1998) (negligence claims against manufacturer of pool component part barred since claims based on failure of contractor to complete pool on time); *Indelco, Inc. v. Hanson Indus. N. Amer.-Grove Worldwide*, 967 S.W.2d 931, 932-33 (Tex. App.—Houston [14th Dist.] 1998, pet. denied) (economic loss due to defective product damaging itself recoverable under contract action, not tort); *Thomson v. Espey Huston & Assocs., Inc.*, 899 S.W.2d 415, 421-22 (Tex. App.—Austin 1995, no writ) (recovery for negligent performance of a contract by engineering firm allowed under contract law, not tort, unless negligence caused damage beyond subject of contract itself).

Texas courts have continued to impose the economic loss rule in other situations as well: *D.S.A., Inc. v. Hillsboro Indep. Sch. Dist.*, 973 S.W.2d 662, 663-64 (Tex. 1998) (per curiam) (economic loss rule precluded recovery under negligent misrepresentation claim); *Crawford v. Ace Sign, Inc.*, 917 S.W.2d 12, 14 (Tex. 1996) (per curiam) (nonperformance of contract was not actionable under DTPA); *Trans-Gulf Corp. v. Performance Aircraft Serv., Inc.*, 82 S.W.3d 691, 695 (Tex. App.—Eastland 2002, no pet.) (economic loss rule barred recovery for negligent repair work when the only damages claimed were economic); *Coastal Conduit & Ditching, Inc. v. Noram Energy Corp.*, 29 S.W.3d 282, 290 (Tex. App.—Houston [14th Dist.] 2002, no pet.) (economic loss rule prevented recovery

of additional expenses incurred as the result of a gas company failure to mark gas lines when the gas company owed no duty and there was no personal injury or property damage); *Weber v. Domel*, 48 S.W.3d 435, 436-37 (Tex. App.—Waco 2001, no pet. h.) (economic loss rule precludes award of exemplary damages in cases over breach of lease); *Facciolla v. Linbeck Constr. Corp.*, 968 S.W.2d 435, 448-49 (Tex. App.—Texarkana 1998, no pet.) (economic loss rule precludes recovery of identical damages under fraud and contract claims); *Equistar Chemicals, L.P. v. Dresser-Rand Co.*, 123 S.W.3d 584, 589-91 (Tex. App. [14th Dist.] 2003, pet. filed) (holding economic loss rule precludes recovery of purely economic losses where limitations had run on implied warranty claims).

The economic loss rule can also arise when a party to a contract for goods sues under a products liability theory to recover its economic damages, such as business interruption losses, damages that are considered purely economic loss. See *Mid-Continent Air Craft Corp. v. Curry County Spring Serv., Inc.*, 572 S.W.2d 308, 312-13 (Tex. 1978). In the commercial context, if damage to “other property” occurred, even if very slight compared to the economic loss, courts would still allow parties to recover their damages under tort law, even though the warranty had long since run. Now, however, Texas courts are beginning to hold that claimants cannot recover their purely economic damages under a tort theory but that these must be recovered under the contract from which they arose. See *Murray v. Ford Motor Co.*, 97 S.W.3d 888 (Tex. App. – Dallas 2003, no pet.); see also, *Equistar*, 123 S.W.3d at 590. If the parties failed to negotiate a longer warranty, then their claims for these damages will be time-barred after four years. *Equistar*, 123 S.W.3d at 590. This trend is consistent with making commercial parties look to the U.C.C. for their remedies. *Id.*

#### 6. Reasonable Certainty and Legal Sufficiency

Because contract damages are composed of economic damages, they can be calculated with reasonable certainty. See *Murdock v. Hospital*, 946 S.W.3d 836, 841 (Tex. 1997). Thus, there must be evidence of the entire amount awarded in order for there to be legally sufficient evidence to support that award. See *id.*; *Formosa*, 960 S.W.2d at 51-52. This objection should be made as a no-evidence objection. *Formosa*, 960 S.W.2d at 44. If damages are contested, the remedy is a new trial. *Id.*

The law distinguishes between uncertainty as to the amount of damages and uncertainty as to the existence of damages. *Id.* If the existence of damages is uncertain, then they are not recoverable. *Id.* Conversely, uncertainty as to amount does not bar a party’s recovery. *Id.*; see also *Vance v. My Apartment Steak House of San Antonio, Inc.*, 677 S.W.2d 480, 484

(Tex. 1984) (finding that where evidence raised question of fact as to costs of repair, jury should have been permitted to determine what repairs were necessitated by breach of contract); see also *Texas Sanitation Co. v. Marek*, 381 S.W.2d 710, 715-17 (Tex. Civ. App.—Corpus Christi 1964, no writ) (upholding jury’s answer to damage issue as supported by evidence).

Parties defending a claim of lost profits often assert that they are uncertain as to existence, citing *Texas Instruments’* standards:

1. Uncertain or changing market conditions;
2. Changing business support;
3. Promotion of invested products;
4. Entry into unknown or unavailable markets;
5. Success of a new and unproven activity.

#### 7. Jury Discretion in Awarding Damages

Challenging contract damages on appeal can conflict with the thought that a jury has discretion to award damages within the “range” of evidence presented at trial. See *Gulf States Util. Co. v. Low*, 79 S.W.3d 561, 566 (Tex. 2002); *Duggan v. Marshall*, 7 S.W.3d 888, 893 (Tex. App. – Houston [1st Dist.] 1999, no pet.); *Howell Crude Oil Co. v. Donna Refinery Partners, Ltd.*, 928 S.W.2d 100, 108 (Tex. App. – Houston [14th Dist.] 1996, writ denied). An issue of legal sufficiency arises if either the “high” or “low” estimated damage amounts are not supported by legally sufficient evidence, such as if one or the other is based on gross, and not net, lost profits. See, e.g., *Texaco, Inc. v. Ngyen*, 137 S.W.3d 763 (Tex. App. – Houston [1st Dist.] 2004, no pet. h.). In this case, although unclear, it seems that although the jury has discretion to choose between figures that are supported by legally sufficient evidence, that discretion does not extend to numbers that are not supported by legally sufficient evidence. But see *F.S. New Prods. v. Strong Indus.*, 129 S.W.3d 606, 624-26 (Tex. App. – [1st Dist.] 2004, pet. filed). Another issue is whether, if there is no objection to a failure to include an instruction on the measure of damages, the jury can award any amount that it wants. See *id.* Finally, charge issues may arise if an element of damages unsupported by legally insufficient evidence is included in a broad form jury question with proper damage claims. *Harris County v. Smith*, 96 S.W.3d 230, 234 (Tex. 2002).

#### H. Contract Defenses

##### 1. Repudiation or Anticipatory Breach of Contract

Repudiation or anticipatory breach is a positive and unconditional refusal to perform the contract in the future, expressed either before or after partial performance. *Van Polen v. Wisch*, 23 S.W.3d 510, 516 (Tex. App. – Houston [1st Dist.] 2000, pet.

denied); *see Group Life & Health Ins. Co. v. Turner*, 620 S.W.2d 670, 673-74 (Tex. Civ. App.—Dallas 1981, no writ) (explaining that where insurer stopped paying insured's monthly disability payments and refused to reconsider position, insurer repudiated contract). Repudiation is conduct that shows an unconditional fixed intention, declared in positive terms, to abandon, renounce, and refuse to perform the contract. *In re Braddock*, 64 S.W.3d 581, 585 (Tex. App. – Houston [1st Dist.] 2000, pet. denied).

Complete repudiation entitles the non-breaching party to immediately make a claim, maintain a suit for damages caused by the entire breach, including expectancy damages. *Murray v. Crest Constr., Inc.*, 900 S.W.2d 342, 344 (Tex. 1995) (per curiam). Thus, Texas courts permit the non-breaching party in an installment contract to sue for all future payments. *Turner*, 620 S.W.2d at 673-74; *Pollack*, 39 S.W.2d at 855.

If a party repudiates before performance is due, the repudiating party may retract the anticipatory breach by notifying the promisee of its intent to perform. *Glass v. Anderson*, 596 S.W.2d 507, 510 (Tex. 1980). However, no right to retract the repudiation is available if the other party sues on the contract or materially changes position in reliance on the initial repudiation. *Griffith v. Porter*, 817 S.W.2d 131, 135 (Tex. App.—Tyler 1991, no writ) (“If the repudiation is not accepted by the other party, the contract is kept alive for the benefit of both parties....”); *Valdina Farms, Inc. v. Brown, Beasley & Assocs., Inc.*, 733 S.W.2d 688, 692-93 (Tex. App.—San Antonio 1987, no writ) (finding no anticipatory breach where defendant retracted alleged repudiation and plaintiff failed to show that it materially changed its position in reliance on the repudiation); *Helsley v. Anderson*, 519 S.W.2d 130, 133 (Tex. Civ. App.—Dallas 1975, no writ) (holding repudiation of contract was timely retracted on contract to convey property, since both parties indicated willingness to complete transaction, vendor did not change his position in reliance upon possible repudiation, and no obligation to perform had matured).

## 2. Promissory Estoppel

Promissory estoppel provides that a promise may be binding if the promisor should reasonably expect that his promise will induce action or forbearance, the promisee substantially relies upon the promise, and the enforcement of the promise is necessary to avoid injustice. *Adams v. Petrade Int'l, Inc.*, 754 S.W.2d 696, 707 (Tex. App.—Houston [1st Dist.] 1988, writ denied) (citing “*Moore*” *Burger, Inc. v. Phillips Pet. Co.*, 492 S.W.2d 934, 937 (Tex. 1972)). This doctrine is often used by both parties in a contract action as a plea. *Adams*, 754 S.W.2d at 707; *Kenney v. Porter*, 604

S.W.2d 297, 304 (Tex. Civ. App.—Corpus Christi 1980, writ ref d n.r.e.).

Promissory estoppel may also bar the application of the statute of frauds to an otherwise unenforceable oral agreement. *Exxon Corp. v. Breezevale Ltd.*, 82 S.W.3d 429, 438 (Tex. App.—Dallas 2002, pet denied.). Where there is an oral promise to sign an agreement which must be in writing, the written agreement must be in existence at the time the oral promise to execute the same is made; otherwise, promissory estoppel does not apply. *Id.*

A party can recover reliance damages, but not expectancy damages under promissory estoppel. *Fretz Constr. Co. v. Southern Nat'l Bank*, 626 S.W.2d 478, 483 (Tex. 1981); *accord Sun Oil Co. v. Madeles*, 626 S.W.2d 726, 734 (Tex. 1981). Lost profits are not allowable under a promissory estoppel theory of recovery. *Fretz Constr. Co.*, 626 S.W.2d at 483.

Finally, a party asserting promissory estoppel must plead and prove the defense or it is waived. TEX. R. CIV. P. 94. If a party introduces evidence on its elements it should request a specific question on the claim (or defense) in writing to the court. If the court refuses, counsel should object at the charge conference and get a written ruling or an oral ruling on the record. *State Dept. of Highways & Public Transportation v. Payne*, 838 S.W.2d 235 (Tex. 1992).

## III. COVENANTS NOT TO COMPETE

The Texas Business and Commerce Code governs covenants not to compete. *See* TEX. BUS. & COMM. CODE § 15.50, *et seq.* (The Covenants Not to Compete Act).

### A. Enforceability

A covenant not to compete is enforceable if it is ancillary to or part of an otherwise enforceable agreement at the time it is made and it contains limitations as to time, geographical area, and scope of activity to be restrained that are reasonable and do not impose a greater restraint than is necessary to protect the good will or other best interest of the promisee. *Light v. Centel Cellular Co.*, 883 S.W.2d 642, 647 (Tex. 1994). To be ancillary to an enforceable agreement, the consideration that the employer gives must be non-illusory and give rise to the employer's interest in restraining the employee from competing and the covenant must be designed to enforce the employee's consideration or return promise. *Id.* If the covenant is too broad, the court is under a statutory duty to reform the covenant. TEX. BUS. & COM. CODE § 15.51(c); *Butler v. Arrow Mirror & Glass, Inc.*, 51 S.W.3d 787, 793-94 (Tex. App. – Houston [1st Dist.] 2001, no pet.). Because the court will decide as a matter of law whether a covenant is enforceable, counsel can preserve complaints of unenforceability by moving for summary judgment, directed verdict, and

j.n.o.v. Specific objections should be made as to why the covenant is overbroad and must be reformed. *State Dept. of Highways & Public Transportation v. Payne*, 838 S.W.2d 235 (Tex. 1992).

## B. Types of Available Relief

A party can recover monetary damages, injunctive relief, or both when the other contracting party breaches a valid covenant not to compete. TEX. BUS. & COM. CODE ANN. § 15.51(a) (Vernon 2002). A covenant not to compete is a restraint of trade and will not be enforced unless it is reasonable. *Light*, 883 S.W.2d at 647. Whether a covenant not to compete is enforceable is a question of law. *Id.*

### 1. Monetary Damages

The usual measure of monetary damages is equal to the amount of the promisee's lost profits caused by the competition. Because it is difficult to establish damages in a breach of noncompetition contract, courts allow recovery of monetary damages based upon evidence that will enable a jury to make a fair and reasonable approximation of damages. *Arabesque Studios, Inc. v. Academy of Fine Arts Int'l, Inc.*, 529 S.W.2d 564, 569 (Tex. Civ. App.—Dallas 1975, no writ). Such awards do not have to be mathematically exact, but cannot be based upon mere speculation or conjecture. *Id.*

#### a. Proof of monetary damages

A jury may consider several factors in determining a buyer's damages due to a seller's breach of a covenant not to compete pursuant to the sale of a business, such as profits made by the sellers following a breach, profits made prior to the breach, evidence comparing the profitability of two competing businesses, or comparing profits of the injured business before and after the breach. *Chandler v. Mastercraft Dental Corp*, 739 S.W.2d 460, 466 (Tex. App.—Fort Worth 1987, writ denied).

#### b. Monetary damages for invalid covenants

A party cannot recover monetary damages for covenants that are unreasonable, overbroad or restrictive. TEX. BUS. & COM. CODE ANN. § 15.51(c). Covenants not to compete must contain limitations as to time, geographical area, or scope of activity to be restrained. Courts should not impose a greater restraint than necessary to protect the goodwill or other business interest of the promisee. TEX. BUS. & COM. CODE § 15.51(c); *Weatherford Oil Tool Co. v. Campbell*, 340 S.W.2d 950, 953 (Tex. 1960). (“[T]he restrictive covenant must bear some relation to the activities of the employee. It must not restrain his activities in a territory into which his former work has not taken him or given him the opportunity to enjoy undue advantages in later competition with his employer.”).

Further, a court may not award damages based on breach of a covenant not to compete that is void and unenforceable before the covenant is reformed. TEX. BUS. & COM. CODE § 15.51(c); *Weatherford*, 340 S.W.2d at 952.

In *Weatherford*, Weatherford sued three of its former employees for breach of a covenant not to compete. *Id.* at 951. The Texas Supreme Court found that the agreement effectively prevented former employees from doing business anywhere in the world as it contained no territorial limitation. *Id.* at 952. The covenant was therefore unenforceable in accordance with its terms. *Id.* Because the employer's action for damages resulting from competition occurred before a court of competent jurisdiction prescribed a reasonable territory, the claim for damages had to “stand or fall on the contract as written.” *Id.* at 953. The court declined to reform the contract,<sup>2</sup> and found that there was no legal basis or an award of damages. *Id.*; see also *Juliette Fowler Homes, Inc. v. Welch Assocs., Inc.*, 793 S.W.2d 660, 662-63 (Tex. 1990) (denying monetary damages for breach of an unenforceable noncompetition clause, because in an action for damages, the enforceability of a covenant not to compete will be determined as written and may not be modified to render it reasonable and enforceable), *superseded in part by statute as stated in Property Tax Assoc., Inc. v. Staffeldt*, 800 S.W.2d 349 (Tex. App.—El Paso 1990, writ denied).

#### c. Liquidated damages for covenants not to compete

A liquidated damages provision in a breach of a noncompetition agreement will be held valid and enforceable if its terms are reasonable. *Peat Marwick Main & Co. v. Haass*, 818 S.W.2d 381, 385 (Tex. 1991); *Henshaw v. Kroenecke*, 656 S.W.2d 416, 419 (Tex. 1983). Liquidated damages must be a reasonable forecast of just compensation for the harm expected as a result of a breach. *Stewart v. Basey*, 245 S.W.2d 484, 486-87 (Tex. 1952) (holding where lease contract provision, if breached, provided for payment of damages for each and every month of unexpired lease term, provision was unenforceable), *superseded by statute as stated in McFadden v. Fuentes*, 790 S.W.2d 736, (Tex. App.—El Paso 1990, no writ) (referring to the adoption of the UCC and its applicability to the sale of goods); RESTATEMENT OF CONTRACTS § 339

<sup>2</sup> The court noted that although the covenant was unreasonable, a court of equity could have enforced the contact by granting an injunction restraining the former employees from competing for a time and within an area that was reasonable under the circumstances. *Weatherford*, 340 S.W.2d at 952-53. By the time the case reached the Texas Supreme Court, however, the period of noncompetition had expired, rendering the issue of injunctive relief moot. *Id.* at 952.

(1932). Such a provision will only be considered valid if actual damages are difficult to estimate accurately. *See Mayhall v. Proskowetz*, 537 S.W.2d 320, 322 (Tex. Civ. App.—Austin 1976, writ ref d n.r.e.); *Stewart*, 245 S.W.2d at 486. Whether a liquidated damages provision is reasonable is a legal question for a court. *Henshaw*, 656 S.W.2d at 418. If the liquidated damages clause is not reasonable, it is unenforceable as a penalty. *Eberts v. Businesspeople Pers. Servs., Inc.*, 620 S.W.2d 861, 863 (Tex. Civ. App.—Dallas 1981, no writ). Further, liquidated damages are not appropriate in conjunction with actual damages because they are intended as complete relief. *Id.*; *Robert G. Beneke & Co., Inc. v. Cole*, 550 S.W.2d 321, 322 (Tex. Civ. App.—Dallas 1977, no writ) (finding liquidated damages provision providing for payment for breach of a covenant not to compete, but failing to exclude further liability for actual damages, unenforceable as penalty); *see also Phillips v. Phillips*, 820 S.W.2d 785, 788-90 (Tex. 1991) (discussing liquidated damages generally).

Texas Business and Commerce Code section 15.51(c) allows reformation of a covenant not to compete that contains unreasonable limitations by “impos[ing] a greater restraint than is necessary to protect the goodwill or other business interest of the promisee.” TEX. BUS. & COM. CODE ANN. § 15.51(c). However, section 15.51(c) expressly provides, and has been enforced to hold, that “the court may not award the promisee damages for a breach of the covenant before its reformation and the relief granted to the promisee shall be limited to injunctive relief.” *Peat Marwick Main & Co. v. Haass*, 818 S.W.2d 381, 388 (Tex. 1991) (quoting § 15.51(c)); *cf. Butler v. Arrow Mirror & Glass, Inc.*, 51 S.W.3d 787, 797 (Tex. App.—Houston [1st Dist.] 2001, no pet.) (allowing recovery of attorney fees under Texas Civil Practice and Remedies Code section 38.001 despite reformation of covenant not to compete). *But see Perez v. Texas Disposal Sys., Inc.*, 53 S.W.3d 480, 482-83 (Tex. App.—San Antonio 2001, no pet.) (reversing an award of attorney fees to an employer from an employee for violation of a covenant not to compete), *rev'd on other grounds*, 80 S.W.2d 593 (Tex. 2002).

## 2. Injunctive Relief

Covenants not to compete are often enforced with temporary or permanent injunctions.

### a. Temporary injunctions

A temporary injunction's purpose is to preserve the status quo of the litigation's subject matter pending a trial on the merits. *Walling v. Metcalfe*, 863 S.W.2d 56, 57 (Tex. 1993); *Electronic Data Sys. Corp. v. Powell*, 508 S.W.2d 137, 139 (Tex. Civ. App.—Dallas 1974, no writ). A temporary injunction is an extraordinary remedy and does not issue as a matter of

right. *Walling*, 863 S.W.2d at 57. To obtain a temporary injunction, the applicant must plead and prove three specific elements: (1) a cause of action against the defendant; (2) a probable right to the relief sought; and (3) a probable, imminent, and irreparable injury in the interim. *Walling*, 863 S.W.2d at 57; *Sun Oil Co. v. Whitaker*, 424 S.W.2d 216, 218 (Tex. 1968). An injury is irreparable if the injured party cannot be adequately compensated in damages or if the damages cannot be measured by any certain pecuniary standard. *Canteen Corp. v. Republic of Tex. Props., Inc.*, 773 S.W.2d 398, 401 (Tex. App.—Dallas 1989, no writ).

### i. abuse of discretion standard

Whether to grant or deny a temporary injunction is within the trial court's sound discretion. *Walling*, 863 S.W.2d at 58; *State v. Walker*, 679 S.W.2d 484, 485 (Tex. 1984). A reviewing court should reverse an order granting injunctive relief only if the trial court abused that discretion. *Walling*, 863 S.W.2d at 58; *Walker*, 679 S.W.2d at 485. The reviewing court must not substitute its judgment for the trial court's judgment unless the trial court's action was so arbitrary that it exceeded the bounds of reasonable discretion. *Johnson v. Fourth Ct. of Appeals*, 700 S.W.2d 916, 918 (Tex. 1985); *Davis v. Huey*, 571 S.W.2d 859, 861-62 (Tex. 1978).

### ii. interlocutory appeal of temporary injunction

A trial court's granting of a temporary injunction is an interlocutory order subject to immediate appeal. TEX. CIV. PRAC & REM. CODE § 51.014(a)(4). The trial court's decision is reviewed for an abuse of discretion. *Walling v. Metcalfe*, 863 S.W.2d 56, 58 (Tex. 1993). The Court of Appeals may modify an overbroad injunction. *Stone v. Griffin Comm. & Sec. Sys.*, 53 S.W.3d 687, 695 (Tex. App. — Tyler 2001, no pet.). Note, however, that an interlocutory appeal of an order granting a temporary injunction does not stay the trial. TEX. CIV. PRAC & REM. CODE § 51.014(b).

### b. Permanent injunctions

A party seeking a permanent injunction must prove the existence of a probable right to permanent relief and a probably injury. *Manning v. Wieser*, 474 S.W.2d 448, 449 (Tex. 1971). An appellate court reviews a trial court's granting of a permanent injunction under an abuse of discretion standard. *Id.* The appellate court determines whether the trial court's action was so arbitrary as to exceed the bounds of reasonable discretion. *Jones v. Strayhorn*, 159 Tex. 421, 321 S.W.2d 290, 295 (1959).

## 3. Exemplary Damages in Covenants Not to Compete

Just as in all contract cases, exemplary damages are typically unavailable in a breach of a noncompetition agreement case, even if the breach was

committed with malice. *See A.L. Carter Lumber Co. v. Saide*, 140 Tex. 523, 168 S.W.2d 629, 631 (1943) (holding exemplary damages not recoverable in breach of contract to sell land, even though the breach was brought about capriciously and with malice, because the breach was not accompanied by a tort). If, however, the breach was accompanied by a tort, exemplary damages may be recovered if proper culpability is established. *First Sec. Bank & Trust Co. v. Roach*, 493 S.W.2d 612, 618-19 (Tex. Civ. App.—Dallas 1973, writ ref'd n.r.e.) (finding bank's wrongful sequestration of automobile was distinct and independent tort, thereby entitling plaintiff to exemplary damages that take into account lost earnings, mental suffering, doctor bills, and attorney's fees).

#### IV. COMMON LAW FRAUD

A person injured by common law fraud may recover direct and consequential damages. *Formosa Plastics Corp. USA v. Presidio Eng'rs & Contractors, Inc.*, 960 S.W.2d 41, 49 n. 1 (Tex. 1998); *Airborne Freight Corp. v. C.R. Lee Enters., Inc.*, 847 S.W.2d 289, 295 (Tex. App.—El Paso 1992, writ denied); RESTATEMENT (SECOND) OF TORTS § 549 (1977). Exemplary damages also are available in a fraud action, TEX. CIV. PRAC. & REM. CODE ANN. § 41.003(a)(1) (Vernon 1997); *Trenholm v. Ratcliff* 646 S.W.2d 927, 933 (Tex. 1983). Fraud is an attractive theory to claimants in the commercial context because it opens the door to punitive damages and gives them alternate theories of recovery.

##### A. Direct Damages

Texas recognizes two measures of direct damages for common-law fraud: the out-of-pocket measure and the benefit-of-the bargain measure. *Formosa Plastics*, 960 S.W.2d at 49. Direct damages are usually measured by the out-of-pocket loss of the benefit of the bargain. *Id.* Neither the out-of-pocket nor benefit-of-the-bargain theories seem to adequately address all damages issues.<sup>3</sup> In these situations, the plaintiff will be forced to prove special or consequential damages and cannot rely on out-of-pocket or benefit-of-the-bargain damages. *Texas Commerce Bank Reagan*, 865 S.W.2d at 73-74.

<sup>3</sup> One example is when the fraud is not based on the transfer of property or something else of value. *Texas Commerce Bank Reagan v. Lebcu Constructors, Inc.*, 865 S.W.2d 68, 73-74 (Tex. App.—Corpus Christi, 1993, writ denied); *Sanchez v. Johnson & Johnson Med., Inc.*, 860 S.W.2d 503, 514 (Tex. App.—El Paso 1993), *modified on other grounds*, 924 S.W.2d 925 (Tex. 1996).

##### 1. Out-Of-Pocket Damages

Out-of-pocket damages in a fraud case are measured the difference between the value paid by the aggrieved party and the value received. *Formosa Plastics*, 960 S.W.2d at 49; *Fortune Prod. Co. v. Conoco, Inc.*, 52 S.W.3d 671, 681 (Tex. 2000). Several courts have stated that the goal in measuring out-of-pocket damages is to provide actual compensation for injury, not profit. *Duval County Ranch Co. v. Wooldridge*, 674 S.W.2d 332, 335-36 (Tex. App.—Austin 1984, no writ). The theory is that if the plaintiff receives a sum of money that makes what the plaintiff received equal to what was actually conveyed, the plaintiff is made whole. *George*, 93 S.W. at 108.

##### 2. Benefit-of-the-Bargain

For a discussion on benefit-of-the-bargain damages, please refer to section II.A.1.

##### 3. Fair Market Value

Fair market value is a common formula used to measure the value of damages. *Morriss-Buick Co. v. Pondrom*, 131 Tex. 98, 113 S.W.2d 889, 890 (1938); *Traylor v. Gray*, 547 S.W.2d 644, 657 (Tex. Civ. App.—Corpus Christi 1977, writ ref d n.r.e.). Such damages are generally measured as of the time of the transaction. *Arthur Andersen & Co*, 945 S.W.2d at 817; *Leyendecker & Assocs., Inc. v. Wechter*, 683 S.W.2d 369, 373 (Tex. 1984). The fair market value is defined as the price at which the thing of value would change hands between a willing seller, under no compulsion to sell, and a willing buyer, under no compulsion to buy, with both parties having reasonable knowledge of relevant facts. *Fisher v. Yates*, 953 S.W.2d 370, 379 (Tex. App.—Texarkana 1997, pet. denied); *State Nat'l Bank v. Farah Mfg. Co., Inc.*, 678 S.W.2d 661, 697 (Tex. App.—El Paso 1984, writ dism'd by agr.). The definition of fair market value presupposes an existing and established market. *State Nat'l. Bank*, 678 S.W.2d at 697. However, the time of the transaction is not appropriate in all situations. *See, e.g., Traylor*, 547 S.W.2d at 657 (finding in futures contract, proper measure was fair market value of cotton at time of misrepresentation less the future market value at the time of the maturity of the crop).

#### V. STATUTORY FRAUD

##### A. Generally

Statutory fraud is limited to transactions in real estate or stocks. TEX. BUS. & COM. CODE ANN. § 27.01 (Vernon 2002). Statutory fraud does not apply to transactions that only tangentially involve land or stocks. *Texas Commerce Bank Reagan v. Lebcu Constructors, Inc.*, 865 S.W.2d 68, 82 (Tex. App.—Corpus Christi 1993, writ denied). Actual damages are recoverable for statutory fraud. TEX. BUS. & COM.

CODE § 27.01(b). Unlike common law fraud, a successful statutory fraud plaintiff may also recover reasonable and necessary attorneys' fees, expert witness fees, and costs for copies of depositions in addition to costs of court. *Id.* § 27.01(e); *Maeberry v. Gayle*, 955 S.W.2d 875, 881 (Tex. App.--Corpus Christi 1997, no pet.). The plaintiff may recover exemplary damages from either the person who made the false representation or the person who benefits from the false representation if either had actual awareness of the falsity. TEX. BUS. & COM. CODE § 27.01(c), (d). Actual awareness may be inferred where objective manifestations indicate that a person acted with actual awareness. *Id.*

Prior to the 1983 amendment to the statutory fraud cause of action, actual damages were defined as the "difference between the value of the real estate or stock as represented or promised, and its actual value in the condition in which it is delivered at the time of the contract." Act of Sept. 1, 1967, 60th Leg., R.S., ch. 785, § 1, 1967 Tex. Gen. Laws 2343, 2603 (amended 1983) (current version at TEX. BUS. & COM. CODE ANN. § 27.01 (Vernon 2002)). The former statutory definition is the same as benefit-of-the-bargain damages under the common law. *See Formosa Plastics Corp. USA v. Presidio Eng'rs & Contractors, Inc.*, 960 S.W.2d 41, 49 (Tex. 1998). However, the statute is now silent as to how actual damages are measured for statutory fraud. *See* TEX. BUS. & COM. CODE ANN. § 27.01(b). Thus, a statutory fraud plaintiff can now recover either benefit-of-the-bargain damages or out-of-pocket damages plus any consequential damages under the general definition of actual damages. *Scott v. Sebree*, 986 S.W.2d 364, 368-69 (Tex. App. -- Austin 1999, pet. denied) (interpreting actual damages as used in section 27.01(c) to include those damages available for common law fraud); *Arthur Andersen & Co. v. Perry Equip. Co.*, 945 S.W.2d 812, 816 (Tex. 1997) (actual damages include direct and consequential damages); *Kerrville HRH, Inc., v. City of Kerrville*, 803 S.W.2d 377, 386-87 (Tex. App.--San Antonio 1990, writ denied) (awarding out-of-pocket and consequential damages); *El Paso Dev. Co. v. Ravel*, 339 S.W.2d 360, 363 (Tex. Civ. App. -- El Paso 1960, writ ref'd n.r.e.) (out-of-pocket and consequential damages available under former statute).

### B. Statutory Fraud Damages Cases

The following cases are representative of damage awards in statutory fraud causes of action:

- *McDonald v. Bennett*, 674 F.2d 1080 (5th Cir. 1982) (applying Texas law).

The plaintiff purchased a majority of the stock of a closely held corporation based on

misrepresentations as to the corporation's financial status. The court recognized that section 27.01 of the Texas Business and Commerce Code provided for the award of actual damages as measured by the benefit-of-the-bargain. *McDonald*, 674 F.2d at 1089-90. However, it further declared that out-of-pocket and consequential damages also were recoverable notwithstanding the statute. *Id.* at 1090.

The plaintiff offered evidence as to the value of the stock as represented by the defendants. *Id.* He also offered evidence that the stock did not have any value given the financial condition of the company. *Id.* Accordingly, the jury awarded the difference between the value represented and zero. *Id.* The court held that this was a proper benefit-of-the-bargain measure of damages and was supported by the evidence. *Id.* However, as the jury awarded benefit-of-the-bargain damages for common law fraud associated with the same acts, the plaintiff was not entitled to a double recovery. *Id.*

- *Schlumberger Tech. Corp. v. Swanson*, 959 S.W.2d 171 (Tex. 1997).

In this case, consultants for an offshore diamond mining project filed suit against the defendant corporation alleging, among other things, statutory fraud. *Id.* at 175. Plaintiffs had originally entered into a letter agreement with an entity which, through various mergers and acquisitions, transferred its interest in the project to a subsidiary of the named defendant. *Id.* at 173-74. After the project had operated for some time the defendant represented to the plaintiffs that the diamond project was neither technologically feasible nor commercially viable. *Id.* at 174. As a result, the plaintiffs, who were at all times represented by counsel, agreed to sell their interest to the defendant for approximately \$814,000. *Id.* In exchange, the plaintiffs agreed to relinquish all rights, claims, and interests in the project, and further released all causes of action against the defendant, known or unknown. *Id.* Moreover, the plaintiffs specifically agreed that they were not relying on any statement or representation of defendant, that they were relying on their own judgment, and that they had been represented by counsel. *Id.* Defendant thereafter sold the project for approximately \$4.1 million. *Id.*

After a trial on the merits, the jury returned a verdict awarding the plaintiffs \$15 million in actual damages and \$35 million in exemplary

damages on their statutory fraud claim. *Id.* at 174-75. The trial court rendered a judgment notwithstanding the verdict based on the release, but the court of appeals reversed and rendered judgment in accordance with the jury's findings. *Id.* at 175. The Texas Supreme Court held that the release precluded all of the plaintiffs' claims as a matter of law, and rendered judgment for the defendant. *Id.*

- *White v. Bond*, 362 S.W.2d 295 (Tex. 1962).

This statutory fraud case arose out of the sale of stock in a uranium mining company. *Id.* at 295. The court relied on the prior statute's definition of actual damages: that is, the difference between the value of the stock as represented and the actual value of the stock. *Id.* at 297. Here, the evidence was not sufficient to support an award of actual damages. The court recognized that from the testimony, the jury might have properly inferred that the shares of stock had little or no value at the time of the purchase. However, the record was wholly silent as to what value the stock would have had if the representations had been true. *Id.* Evidence that: (1) the plaintiffs had been offered a special deal; (2) that the defendant was going to sell shares to the public at a later time at ten times the amount the plaintiff paid; and, (3) that the defendant had represented that the plaintiffs could reasonably expect to get three to four times the amount paid if they sold their stock in the future was no evidence of the market value of the stock even if the representations had been true. *Id.*

- *Williams v. Gaines*, 943 S.W.2d 185 (Tex. App.--Amarillo 1997, writ denied).

In *Williams*, the court found that the evidence presented by the plaintiff to establish the fair market value of the stock in a brand new corporation was insufficient to support a jury award of \$92,500. *Id.* at 192-93. The plaintiff's expert testified that the two recognized methods to determine the fair market value of a corporation were the "asset method" and the "earnings method". He based his opinion on the earnings method, claiming that it was more appropriate because the corporation at issue was a service company and did not have many assets. *Id.* at 192. The allegations of fraud centered on the defendant's failure to transfer fifty percent of the shares of a new corporation to plaintiff in exchange for a valuable contract.

The plaintiff's expert utilized only seven months of income and operations data from the corporation because it had been in operation for such a short time. *Id.* The expert indicated that the company had shown a net profit of \$101,754. He testified that in his opinion the net profit should have been \$147,754, but did not explain why. Taking this information along with cash flow information, the expert concocted a fair market value of \$618,000 for the stock and thus concluded that one half of the value of the stock should be \$309,000. *Id.* Nevertheless, the expert admitted that the book value of the corporation was less than zero. *Id.*

Because the corporation had never sold its stock, there was no evidence of market value of the stock by its sales. The court noted that the book value of a corporation is entitled to little weight, if any, in determining the value of the corporate stock. *Id.* When the value of the stock cannot be shown by sales, valuation is ordinarily based on the market value of the assets of the company after deducting its liabilities. *Id.* at 193. As the expert failed to base his opinion on the assets and liabilities of the corporation, his testimony was insufficient to establish the market value of the stock. *Id.* Furthermore, the expert failed to base his testimony on information at the appropriate time. *Id.* According to the court, the expert should have based the value of the stock at the time the fraud was committed. *Id.*

- *Kerrville HRH, Inc. v. City of Ken-villa*, 803 S.W.2d 377 (Tex. App.--San Antonio 1990, writ denied).

This statutory fraud action arose out of a real property lease. The court affirmed an award of out-of-pocket expenses, lost profits and interest expenses arising out of the defendant city's fraud. *Id.* at 389.

The plaintiff leased farm land from the city which was represented to have an adequate irrigation system for the growing of lawn grass and other nursery plants. *Id.* at 383. The irrigation system did not work. *Id.* at 383-84. Plaintiff attempted repairs which proved unsuccessful. *Id.* at 381. Plaintiff offered testimony that by the time of trial, plaintiff had spent \$360,509.15 on rent, labor, equipment leases and purchases, fuel and oil, utilities, taxes, legal fees, insurance and plants. *Id.* at 386. Of the approximately \$360,000 in damages, the plaintiff included \$82,691.62 in interest payable as of the date of trial on a bank

loan taken out by the plaintiff to fund its business. *Id.*

With respect to lost profits, the sales prices of the plaintiff's products were well established, and the plaintiff offered testimony that there was a market demand in Texas for its products. *Id.* at 387. For example, each tree would sell for \$35 within a year. Taking this figure, the plaintiff projected its net profit on trees and shrubs over the life of the lease to be \$ 1.297 million. *Id.* It also projected net profit on the grass at \$239,000. *Id.* The jury awarded \$246,167.53 in out-of-pocket expenses, \$25,000 in lost profits and zero dollars in interest. *Id.*

The court held that the out-of-pocket expenses were established by the evidence and given the speculative nature of future profits, the \$25,000 in lost profits was also appropriate. *Id.* Given the fact that the plaintiff had offered evidence of the existence of its loan and the amount of interest due, there was no basis for the jury's answer of zero with respect to the interest, and the court accordingly increased the plaintiff's award of damages. *Id.*

- *How Ins. Co. v. Patriot Financial Services*, 786 S.W.2d 533 (Tex. App.--Austin 1990, writ denied), *overruled on other grounds sub nom*, 843 S.W.2d 464 (Tex. 1992).

Under section 27.01(b) of the Texas Business and Commerce Code, a defrauded person may recover "actual damages." In this case, the court relied on a 1960 decision to interpret "actual damages" as "such damages as result directly, naturally and proximately from fraud." *How Ins.*, 786 S.W.2d at 546 (citing *El Paso Day. Co. v. Ravel*, 339 S.W.2d 360, 364 (Tex. Civ. App.--El Paso 1960, writ ref d n.r.e.)). At least in a defective construction case, the measure of damages may be either the "difference in value" measure or the "remedial" or "cost to repair" measure of damages. *Id.* Generally, a plaintiff is allowed repair costs if those costs are feasible and do not involve economic waste. *Id.* If they do involve economic waste, the plaintiff is limited to the difference in value measure of damages. *Id.*

The difference of value measure of damages is the difference between the purchase price of the property and the market value of the property at the time of the sale. *Id.* Essentially, this is the out-of-pocket measure of damages. In *How Ins.*, there was undisputed evidence that the condominium's

purchase price was \$97,650. All of plaintiff's witnesses testified as to the market value of the property at the time of trial. This evidence was not sufficient to establish market value at the time of the sale. *Id.*

With respect to exemplary damages under statutory fraud, a plaintiff is entitled to recover such damages if the tortfeasor made the false representation with actual awareness of the falsity. *Id.* at 545. In this case, the evidence was sufficient to find actual awareness. The builder had accepted bids that were disproportionately low, which the court found was an indicator that the subcontractor might not perform quality work. *Id.* Furthermore, the condominium's architect testified that the builder changed the design specifications for the project because the specifications had become economically unfeasible. *Id.* The architect also testified that he did not recommend the substitutions for the exterior walls and that he had informed the builder of improper installation. *Id.* Finally, the builder had filed an independent lawsuit against the subcontractor responsible for the defects in the plaintiff's home. *Id.*

## VI. CONSTRUCTIVE FRAUD

Constructive or legal fraud is the breach of some legal or equitable duty which, irrespective of moral guilt, the law declares fraudulent because of its tendency to deceive others, to violate confidence or to injure public interest. *Archer v. Griffith*, 390 S.W.2d 735, 740 (Tex. 1964). Constructive fraud does not require an intent to defraud. *Canies v. Meador*, 533 S.W.2d 365, 372 (Tex. Civ. App. — Dallas 1976, writ ref d n.r.e.). Plaintiffs in constructive fraud cases generally seek rescission of some bargain or the return of property fraudulently obtained. *Id.* See, e.g., *Texas Bank Sc Trust Co. v. Moore*, 595 S.W.2d 502, 505 (Tex. 1980).

Exemplary damages are recoverable in appropriate cases, most of which involve the finding of a breach of a fiduciary duty. See, e.g., *Moore*, 595 S.W.2d at 508; *InterFirst Batik Dallas, N.A. v. Risser*, 739 S.W.2d 882, 907 (Tex. App.—Texarkana 1987, no writ); *Kirby v. Ouce*, 688 S.W.2d 161, 166-67 (Tex. App.—Dallas 1985, writ ref d n.r.e.).

## VII. NEGLIGENT MISREPRESENTATION

### A. Elements

The elements of negligent misrepresentation are: (1) representations made by defendant in the course of his business, or in a transaction which he has a pecuniary interest; (2) the defendant supplies false information for the guidance of others and their business; (3) the defendant did not exercise reasonable

care or competence in obtaining or communicating the information; and (4) the plaintiff suffers pecuniary loss by justifiably relying on the representation. *Federal Land Bank v. Sloane*, 825 S.W.2d 439, 442 (Tex. 1991).

### B. Pecuniary Damages

Texas has adopted the measurement of damages as set out by the Restatement (Second) of Torts for negligent misrepresentation. *Federal Land Bank*, 825 S.W.2d at 442. The plaintiff may recover its pecuniary loss including: (1) the difference in value of what the plaintiff received in the transaction and its purchase price or other value given for it, and (2) other consequential damages that can properly be classified as pecuniary losses. *Id.*; RESTATEMENT (SECOND) OF TORTS § 552B (1977).

Mental anguish damages are not available in a negligent misrepresentation case. *Federal Land Bank*, 825 S.W.2d at 442-43. The Restatement also excludes benefit-of-the-bargain damages incurred as a result of reliance on the misrepresenting damages as an available measure of damages. *Id.* at 442; *Ludlow v. DeBerry*, 959 S.W.2d 265, 276 (Tex. App.—Houston [14th Dist.] - 1997, no pet). Therefore, one may not recover lost profits related to the transaction. *Federal Land Bank*, 825 S.W.2d at 443; *Tex. Commerce Bank Reagan v. Lebco Constructors, Inc.*, 865 S.W.2d 68, 75-76 (Tex. App.—Corpus Christi 1993, writ denied) (holding that lost profits are not recoverable as consequential damages for negligent misrepresentation).

### C. Independent Injury Required

In *D.S.A., Inc. v. Hillsboro Indep. Sch. Dist.*, the Texas Supreme Court addressed whether the elimination of the independent injury requirement as stated in *Formosa* extended to claims for negligent misrepresentation or negligent inducement. 973 S.W.2d 662 (Tex. 1998). The school district sued a construction management firm for breach of contract, negligent and gross negligent misrepresentation, and DTPA violations. *Id.* at 663. The district's claims stemmed from faulty work performed on an elementary school construction project. *Id.* The jury returned findings against D.S.A., awarding the district \$260,661 in actual damages, \$170,000 in exemplary damages, plus attorneys' fees. *Id.*

The supreme court held that the damages awarded by the jury for negligent misrepresentation were identical to the damages awarded for breach of contract, and the district failed to offer proof of any injury independent of contract damages. *Id.* The district argued that *Formosa* permitted it to recover in tort for losses related to the subject matter of the contract because D.S.A. had a legal duty, independent from its contractual duties, not to make misrepresentations to

induce the district into the contract. *Id.* The court held that *Formosa's* rejection of the independent injury requirement in fraudulent inducement cases does not extend to claims for negligent misrepresentation or negligent inducement, reasoning that the elimination of the independent injury requirement for negligent misrepresentation claims would, "potentially convert every contract interpretation dispute into a negligent misrepresentation claim." *Id.* at 664. See *MCN Energy Enters, Inc. v. Omagro De Colombia, L.D.C.*, 98 S.W.3d 766, 772 (Tex. App. — Fort Worth 2003, no pet.) (holding that obligations and duties separately imposed by contract and by tort may co-exist, and the Texas Supreme Court's holding in *D.S.A.* did not alter that principle).

## VIII. TORTIOUS INTERFERENCE WITH EXISTING CONTRACT

### A. Elements

A tortious interference cause of action is proven by:

- 1) the existence of a contract subject to interference;
- 2) a willful and intentional act of interference;
- 3) the act was a proximate cause of the plaintiff's damages; and
- 4) actual damage or loss resulted.

*Prudential Ins. Co. of Am. v. Financial Review Serv. Inc.*, 29 S.W.3d 74, 77 (Tex. 2000) (citing *ACS Investors, Inc. v. McLaughlin*, 943 S.W.2d 426, 430 (Tex. 1997)); *Texas Beef Cattle Co. v. Green*, 921 S.W.2d 203, 210 (Tex. 1996).

### B. Actual Damages

The general measure of damages for tortious interference with a contract is the same as the measure of damages for breach of contract-- namely, attempting to put the plaintiff in the same economic position as if the contract had been fully performed. *American Nat. Petroleum Co. v. Transcontinental Gas Pipe Line Corp.*, 798 S.W.2d 274, 278 (Tex. 1990); *Anderson, Greenwood & Co. v. Martin*, 44 S.W.3d 200, 219 (Tex. App. —Houston [14th Dist.] 2001, pet. denied). A successful plaintiff in a suit for tortious interference with contract may be entitled to recover

- the pecuniary loss of the benefit of the contract or the prospective relation;
- consequential losses for which the interference is the legal cause; and
- emotional distress or actual harm to reputation, if they are reasonably to be expected to result from the interference.

*Exxon v. Allsup*, 808 S.W.2d 648, 660 (Tex. App.—Corpus Christi 1991, writ denied) (citing RESTATEMENT (SECOND) OF TORTS § 774A (1977)).

There is no requirement that the loss incurred be one contemplated by the parties to the contract itself at the time the contract was made. *Id.*; see also *Sulzer Carbomedics v. Or. Cardio-Devices, Inc.*, 257 F.3d 449, 455-56 (5th Cir. 2001) (applying Texas law) (holding that a claim for interference with contract is one in tort and damages are not based on contract rules; therefore, it is not required that the loss incurred be one within the contemplation of the parties to the contract itself at the time the contract was made).

### C. Unjust Enrichment As the Measure of Lost Profit Damages

An unjust enrichment measure of damages is appropriate for willful interference with contractual relations, where the plaintiff's lost profits are not readily ascertainable. *Sandare Chem. Co., Inc. v. WAKO Int'l, Inc.*, 820 S.W.2d 21, 23 (Tex. App.—Fort Worth 1991, no writ). In *Sandare Chem.*, the defendant counterclaimed for tortious interference with its contractual and business relations because the defendant was not allowed to pursue its plans to manufacture and market a medical diagnostic test while the plaintiff manufactured and marketed a medical diagnostic test. *Id.* The plaintiff contended that the defendant failed to establish that the defendant had suffered damages that were ascertainable at a fixed time. *Id.* The appeals court recognized that the trial court may have determined that any lost profits suffered by the defendant were not readily ascertainable, but no actual finding was necessary when there is evidence of the interfering party's profit. *Id.* at 24. The court noted that Restatement section 774A does not directly address the issue of whether one may recover defendant's profits in the event plaintiff's profits are not readily ascertainable:

If the absence of discussion concerning whether the defendant's profits may constitute the measure of damages when the plaintiff's lost profits are not readily ascertainable means that the Restatement has declined to adopt the rule as we have stated it, then we decline to adopt the Restatement section 774A as the measure of damages when the plaintiffs lost profit is not readily ascertainable because we find it not to be in accord with the authorities, which we find to support the better rule. *Id.*

Accordingly, the court held that in a tortious interference with contract case, the defendant's profits may constitute evidence of the plaintiff's lost profits,

when the plaintiff cannot show with certainty the profits it would have realized in the absence of interference. *Id.* Thus, in a suit to recover lost profits, it is not necessary that the profits be susceptible of exact calculation; rather it is sufficient that there is evidence from which the profits can be determined with a reasonable degree of certainty. *Holt Atherton Indus., Inc. v. Heine*, 835 S.W.2d 80, 84 (Tex. 1992).

In comparison, in *Marcus, Stowell & Beve v. Jefferson Inv. Corp.*, 797 F.2d 227 (5th Cir. 1986) (applying Texas law), the plaintiff was not allowed recovery of more than its actual damages despite defendant's profit from the interference:

Depriving a tortfeasor of its profits serves the policy of discouraging future wrongdoing while at the same time preventing the "unjust enrichment" of a wrongdoer. *Marcus*, 797 F.2d at 231. Recognizing the importance of these policies, several courts outside of Texas have approved, in particular circumstances, an award for tortious interference based on the defendant's profits. *Id.*

Nevertheless, we conclude that under Texas law the district court properly measured MSB's recovery by the amount of actual loss suffered by MSB. *Id.* Texas courts have observed that the aim of awarding damages for tortious interference is the same as that of awarding damages for breach of contract—that is, to place the injured party in the same economic position it would have been in had the contract not been breached.

*Id.* at 231 (citations omitted); but see *Sulzer Carbomedics*, 257 F.3d at 455 (holding that post-*Marcus* Texas law holds that a party found liable for tortious interference with a contract may be liable for injuries that are reasonably to be expected to result from the interference).

### D. Exemplary Damages

To recover exemplary damages in a claim for tortious interference with an existing contract, the plaintiff is usually required to prove "actual malice." *Texas Reef Cattle Co. v. Green*, 921 S.W.2d 203, 210 (Tex. 1996); *Clements v. Withers*, 437 S.W.2d 818, 822 (Tex. 1969). However, actual malice need not be shown to recover compensatory damages for the tort of interference with an existing contractual relationship. *Texas Beef Cattle Co.*, 921 S.W.2d at 210 (stating that Texas courts have distinguished actual malice, which triggers recovery of exemplary damages, from legal malice, which negates the justification defense).

### E. Miscellaneous

The unenforceability of a contract is no defense to an action for tortious interference with its performance. *Sterner v. Marathon Oil Co.*, 767 S.W.2d 686, 689 (Tex. 1989). A similar situation exists with regard to contracts terminable at will. *Id.* (holding that until terminated, a terminable at will contract is valid and subsisting, and third persons are not free to tortiously interfere with it).

The breaching party and the interfering party are jointly and severally liable only for actual damages incurred by the plaintiff. *Armendariz v. Mora*, 553 S.W.2d 400, 406 (Tex. Civ. App.—El Paso 1977, writ ref'd n.r.e.). There is no joint and several liability as to any award for exemplary damages unless the defendants are closely related or where the defendants conspired to violate plaintiff's rights. TEX. CIV. PRAC. & REM. CODE § 41.005 (Vernon 1997); *Warner Communications Inc. v. Keller*, 888 S.W.2d 586, 599 (Tex. App.—El Paso 1994), *rev'd on other grounds*, 928 S.W.2d 479 (Tex. 1996).

Attorneys' fees cannot be recovered in a claim for tortious interference with contract. *Transcontinental Gas v. American Nat'l Petroleum Co.*, 763 S.W.2d 809, 823 (Tex. App.—Texarkana 1988), *rev'd on other grounds*, 798 S.W.2d 274 (Tex. 1989).

### IX. TORTIOUS INTERFERENCE WITH PROSPECTIVE CONTRACTS OR PROSPECTIVE BUSINESS RELATIONS

To recover for tortious interference with the prospective business relations, a plaintiff must prove that the defendant's conduct was independently tortious or wrongful. *Wal-Mart Stores, Inc. v. Sturges*, 52 S.W.3d 711, 726 (Tex. 2001). The plaintiff need not prove an independent tort, but instead that the defendant's conduct would be actionable under a recognized tort. *Id.* To recover damages for tortious interference with prospective business relationships or prospective contracts, one must have sustained actual damages proximately caused by defendant's willful and intentional action. *Exxon v. Allsup*, 808 S.W.2d 648, 659 (Tex. App.—Corpus Christi 1991, writ denied).

#### A. Recoverable Damages

The damages recoverable for tortious interference with business relations, both existing and prospective, are similar to those recoverable for tortious interference with a contract. A plaintiff may recover such damages sustained by him as are a natural and proximate consequence of the interference. *Sulzer Carbomedics v. Oregon Cardio-Devices, Inc.*, 257 F.3d 449, 455-56 (5th Cir. 2001); *Sandare Chem. Co., Inc. v. WAKO Int'l, Inc.*, 820 S.W.2d 21,23 (Tex. App.—Fort Worth 1991, no writ). Likewise, pecuniary and consequential losses similar to those available for

tortious interference with contract are also available as outlined in section 774A of the Restatement (Second) of Torts:

One who is liable to another for interference with a contract or prospective contractual relation is liable for damages for:

- (1) the pecuniary loss of the benefit of the contract or the prospective relation;
- (2) consequential losses for which the interference is the legal cause; and
- (3) emotional distress or actual harm to reputation, if they are reasonably to be expected to result from the interference.

RESTATEMENT (SECOND) OF TORTS § 774A (1977); *Browning-Ferris, Inc. v. Reyna*, 852 S.W.2d 540, 549 (Tex. App.—San Antonio 1992), *rev'd on other grounds*, 865 S.W.2d 925 (Tex. 1993).

In comparing the damages available for interference with *prospective* business relations and those available for *existing* contract or existing business relations, the description of damages for each tort is very similar. "Damages for interference with an existing contract arise when there is an occurrence of actual damages or loss . . . . Damages for interference with prospective business relations arise when actual harm or damage occur as a result of the interference." *Browning-Ferris, Inc.*, 852 S.W.2d at 549 (citing *Juliette Fowler Homes, Inc.*, 793 S.W.2d 660, 664 (Tex. 1990)). A void contract cannot provide the basis for a claim for tortious interference with a prospective contract. *Ralston Purina Co. v. McKendrick*, 850 S.W.2d 629, 639 (Tex. App.—San Antonio 1993, writ denied) (finding that because neither party had necessary permits to import feed into Mexico, prospective contract cannot provide the basis for plaintiffs tortious interference with a prospective contract claim).

#### B. Malice Is Required

A party must prove malice to recover actual damages for tortious interference with business relations. *Champion v. Wright*, 740 S.W.2d 848, 854 (Tex. App.—San Antonio 1987, writ denied). In other words, unless there is some contractual understanding, a party to a business relationship is protected from only malicious or unlawful interference. *Bray v. Squires*, 702 S.W.2d 266, 272 (Tex. App.—Houston [1st Dist.] 1985, no writ).

The malice required to recover for interference with prospective contracts or business relations is not the same as the "actual malice" required for recovery of exemplary damages. In regard to interference with a prospective contract or relationship, malice "is not to

be understood in its proper sense of ill will against a person, but in its legal sense, as characterizing an unlawful act, done intentionally without just cause or excuse.” *Exxon*, 808 S.W.2d at 648; *Bray*, 702 S.W.2d at 272 (“Malice, in its legal sense, characterizes an act with an unlawful purpose, done intentionally, without just cause or excuse. . . . It is not necessary, in such a case, to show that there was ill-will, spite or other evil motives.”).

In *Wal-Mart Stores, Inc. v. Sturges*, the Texas Supreme Court criticized the malice requirement and stated that it overlaps with the defendant’s defense of justification and creates confusion. 52 S.W.3d 711, 717-18 (Tex. 2001). The court held that to recover under the theory a plaintiff must prove that the defendant’s conduct would be actionable under a recognized tort. *Id.*

Defendants should submit a malice question by filing a written question before the charge conference and object if the judge excludes it from the charge. Otherwise, the issue is waived and considered tried by consent.

### C. Recovery of Lost Profits Available

The recovery of future lost profits is available for both tortious interference with existing contracts and tortious interference with prospective business relations. *Browning-Ferris, Inc.*, 852 S.W.2d at 549. In a claim for tortious interference with business relations, it is possible to recover both “lost profits” and “loss of potential profits,” the latter giving regard to future growth of business. *Champion v. Wright*, 740 S.W.2d 848, 856 (Tex. App.—San Antonio 1987, writ denied).

Depending on the nature of the interference with business relations, a plaintiff may recover lost profits of the diminution in his or her business, in addition to damages recoverable under Restatement (Second) of Torts section 774A. “Where the interference involves the acceptance by one party of salable items intended for his competitor, there may be a recovery for loss of profits. Where the result of the interference is to put the plaintiff out of business it has been said that his damages are the difference between the value of his business in the absence of the interference and the amount realized by liquidation.” *Gonzales v. Gutierrez*, 694 S.W.2d 384, 390 (Tex. App.—San Antonio 1985, no writ).

### D. Mental Anguish Damages Recoverable

Although not generally recoverable in an action based on breach of contract, mental anguish damages are an available element of damages for an intentional tort like tortious interference with prospective contracts. *Comstock Silversmiths, Inc. v. Carey*, 894 S.W.2d 56, 58 n.2 (Tex. App.—San Antonio 1995, no writ). It is undecided whether mental anguish damages

are available in a tortious interference action in which economic damages are not found. *Id.* Presumably, this element of damages is available only to natural persons.

### E. Availability of Exemplary Damages

Exemplary damages are available in suits involving claims for tortious interference with prospective contracts. See *Bard v. Charles R. Myers Ins. Agency, Inc.*, 811 S.W.2d 251, 263 (Tex. App.—San Antonio 1991) (explaining that punitive damages do not violate public policy or the due process clause), *rev’d on other grounds*, 839 S.W.2d 791 (Tex. 1992). To recover exemplary damages in this context, malice must be shown. *Id.* Section 41.001 of the Texas Civil Practice and Remedies Code defines the malice required to recover exemplary damages. See TEX. CIV. PRAC. & REM. CODE ANN. § 41.001 (Vernon 1997).

### F. Attorney Fees

Attorneys fees cannot be recovered in a claim for tortious interference with business relations. *American Nat’l Petroleum Co. v. Transcontinental Gas Pipe Line Corp.*, 798 S.W.2d 274, 283 (Tex. 1990).

## X. RECENT COMMERCIAL LAW TRENDS

### A. Texas Supreme Court Cases

In *Miga v. Jensen*, 96 S.W.3d 207 (Tex. 2002), the court decided how to properly measure the damages to be awarded when an option contract for the purchase of stock is violated.

In *Mustang Pipeline Co. v. Driver Pipeline Co.*, 134 S.W.3d 195 (Tex. 2004), the court held that parties are not required to obtain a finding on the materiality of the breach and approved the broad for submission in Texas Pattern Jury Charge 101.2.

In *PPG Indus., Inc. v. JMB/Houston Centers Partners Ltd.*, 47 Tex. Sup. J. 822 (Tex. 2004), the court held that DTPA claims are not assignable and reaffirmed the principle that services do not extend implied warranties.

In *Interstate Contr. Corp. v. City of Dallas*, 135 S.W.3d 605 (Tex. 2004), the court joined the majority view of other states and recognized for the first time pass-through claims, *i.e.*, a contractor’s claim against an owner on a subcontractor’s behalf when there is no privity of contract between the subcontractor and the owner.

In *Bexar County v. Santikos*, No. 03-0471, \_\_\_\_ Tex. S. Ct. J. \_\_\_\_, (August 27, 2004), the court held that in condemnation cases impaired access to remainder property is a compensable special injury only if a material and substantial impairment of access exists as a matter of law. The court also held that diminished market perception is not recoverable in such cases.

**B. House Bill 4**

Changes by House Bill 4 limit the amount of damages a defendant has to pay by factoring in tax loss. The new subchapter states that if a claimant seeks recovery for loss of earnings, loss of earning capacity, loss of contributions of a pecuniary value, or loss of inheritance, the claimant must present evidence of the loss net of any income taxes or unpaid tax liabilities the claimant would have owed on the claimed loss. This new law still leaves many questions open to debate:

1. In personal injury cases, where recovery is not taxable under federal income tax law, does a party have to prove the tax bracket and what would be received after taxes? If so, is expert testimony required?
2. Does the rule apply in cases where the recovery is taxable?
3. If the claimant is a resident of a state with an income tax, how does it affect the required proof?
4. Are federal estate taxes and state inheritance taxes included?