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***Fraudulent Contractual Inducement*; *Contractual Disclaimers*: Contractual disclaimers of reliance bar tort recovery for misrepresentations that induced the agreement.**

***Reversing a Zero Damages Award - Remand v. Rendition*: Legally conclusive evidence that the plaintiff sustained *some* damages authorizes reversal on a liability theory for which the jury awarded zero damages, even if the precise *amount* of damages was not conclusively established.**

***Economic loss rule*: Overlooked or undermined?**

Under Texas law, a merger clause or a general recitation that the parties made no representations not contained in the written contract alone will not bar a fraudulent inducement suit. *Italian Cowboy Partners, Ltd. v. Prudential Ins. Co. of Am.*, 341 S.W.3d 323, 327 (Tex. 2011). A disclaimer of intent to rely can be effective only if the circumstances indicate that the parties really meant it and understood what they were doing. This determination requires consideration of whether:

1) the disclaimer was truly negotiated, not mere boilerplate;
2) the aggrieved party was represented by counsel;
3) the transaction was conducted at "arm's length;"
4) the parties were knowledgeable about business; and
5) the disclaimer's language was clear.

*Id.* at 337 n. 8.

In *International Business Machines Corp. v. Lufkin Industries, LLC*, Justice Boyd, writing for a unanimous court, had "no trouble" concluding that, under these factors, Lufkin should be barred as a matter of law from recovering from IBM for fraudulently inducing Lufkin's business operations software development agreement. IBM represented that its off-the-shelf software would meet 80% of Lufkin's needs and could be easily customized to satisfy the rest. IBM had no idea whether that was actually true. It was hoping to get Lufkin's business first and later figure out how to make the software do what Lufkin needed.

IBM's software was plagued with problems from the outset and its manifold shortcomings disrupted Lufkin's business operations for eighteen months while IBM tried to fix the problems. By the time Lufkin was sufficiently exasperated that it was willing to pull the plug, it was too late to start over.

*To elude the reliance disclaimer, the representation in the agreement must be specific.*

[1] The opinions expressed are solely those of the author. They do not necessarily represent the views of Munsch, Hardt Kopf & Harr, P.C. or its clients.

IBM was rescued from a multi-million dollar judgment for fraudulent inducement because it included in its written procurement agreement a statement that Lufkin was "not relying upon any representation made by or on behalf of IBM that is not specified in the Agreement." This agreement also included an integration clause stating "the Agreement represent[s] the entire agreement between the parties regarding the subject matter and replace any prior oral or written communications."

Lufkin sought to evade the no-reliance and integration clauses by bringing its claims within representations in the Agreement. It pointed to a provision that responded "none" as to whether "Enhancements" were to be developed as part of the project. Lufkin claimed that this affirmed IBM's general claim that the software would meet most of Lufkin's needs "as is." The court rejected this argument. First, the evidence showed that Lufkin knew the software was going to require *some* modification to work as desired. Second, the representation that there would be no enhancements did not "specify" that the software would meet 80% of Lufkin's needs on its initial implementation. To be sufficiently specific for such a representation to have been "included," the contract should have stated a completion date, the amount of time necessary to provide the services requested, the results required or the amount to be charged. It contained no such statements.

*The introductory acknowledgement that IBM formed its understanding of the project goals by exchanging information with Lufkin's employees not enough to render the disclaimer inapplicable.*

An introductory provision in the agreement stated that IBM "recognize[d] the effort Lufkin Industries' staff has expended … to share information about the goals and objectives of this project, current business processes and supporting systems. This exchange is the basis of [IBM's] understanding for this proposal." Rejecting Lufkin's argument that this recital acknowledged the circumstances surrounding the contract formation, the court reasoned it created no escape from the no-reliance clause because it was not an operative term of the contract. If it were, according to the opinion, this recital would make the disclaimers "superfluous." The reference to exchanged information was too general to meet the exception to the general disclaimer.

Neither the "no enhancement" nor "information exchanged" provisions in the contract defeated the disclaimer's enforceability for failing to be clear and unequivocal as required under the *Italian Cowboy* test. These disclaimers were enough to preclude Lufkin's recovery on the jury's verdict finding that IBM fraudulently induced Lufkin to enter the contract and fraudulently enticed Lufkin not to withdraw due to the software's problems.

*The court treats a great weight evidentiary challenge asserting that the evidence conclusively established the fact of damages.*

The opinion left Lufkin with the possibility of recovery, however. In addition to its tort-based fraudulent inducement claims, Lufkin sued for breach of contract. The jury found that IBM breached its contract but awarded no damages for the breach. Lufkin challenged the zero-damages finding as contrary to the great weight of the evidence and to the jury's damages findings for fraudulent inducement. The Supreme Court of Texas has no authority to consider issues asserting that a jury determination was unsupported by factually sufficient evidence or was contrary to the great weigh of the evidence. But it treated Lufkin's challenge as questioning whether the evidence conclusively established that Lufkin sustained *some* damages. It considered that issue to be within its jurisdiction to reverse for findings that are either unsupported by legally sufficient evidence or contrary to facts conclusively established. This generous reading of Lufkin's argument was in keeping with the court's stated preference for deciding cases on substance and not procedural niceties.

*When the evidence conclusively established the fact of damage, a new trial for that theory of recovery is necessary to determine the amount of those damages.*

Moreover, it deemed the evidence conclusive that Lufkin sustained *some* damages in part. The measure of damages for fraud and breach of contract were essentially the same. The jury's finding of some damages for fraud was supported by the evidence and was irreconcilable with its finding of zero damages for breach of contract. Accordingly, the court reversed the case and remanded for a retrial of the breach-of-contract claim.

*The court ignores the economic loss rule and confuses measure of damages for scope of recoverable damages*.

Out-of-pocket loss may be the *measure* of damages both for fraud and breach of contract. But the critical observer could fairly question the court's reasoning equating damages from the fraud with those from a breach of contract. Under the economic loss rule, damages that are within the contemplation of the parties for a contractual breach – i.e., the economic loss – can only be recovered in contract. Tort recovery, on the other hand, is for damages *other than* those recoverable for the breach of contract. The opinion does not recognize this distinction or explain that, while the *measure* might be the same, the losses to which those measures are applied are not. Recently, there have been several cases that ignored the distinction. Is this failure a mere oversight, or a subtle cast of doubt on the continued viability of the economic loss rule? Stay tuned.

***Governmental Immunity From Suit*: *Sabine Pilot*'s recognition of an exception allowing wrongful termination suits by an at-will employee when terminated for refusing to perform an illegal act did not impliedly waive governmental immunity from suit.**

***Illegal Act Exception to At-Will Employment*: The *Sabine Pilot* exception will apply to government as well as private employers.**

*Hillman v. Nueces County* questioned whether governmental immunity from suit applied to a wrongful termination suit against a county. The county allegedly terminated a prosecutor for refusing instructions to withhold exculpatory evidence from a criminal defendant. Justice Boyd, writing for a unanimous court, ruled that the county enjoyed governmental immunity from suit so that the trial court lacked subject-matter jurisdiction.

The court rejected the employee's argument that recognition in *Sabine Pilot Service, Inc. v. Hauck*, 687 S.W.2d 733 (Tex. 1985), impliedly waived immunity from suit. *Sabine Pilot* recognized an exception to the general rule in Texas that a private employer may terminate an at-will employee for any reason without liability. The exception arises when an employee is terminated for refusing to perform an illegal act.

The prosecutor maintained the *Sabine Pilot* exception also applied to governmental entities, not just private employers. He urged that his termination was for refusing to engage in unlawful conduct because he was ethically obligated to divulge the exculpatory information. On this basis, the prosecutor concluded that meaningful application of the *Sabine Pilot* exception to a governmental employer also required waiver of immunity from suit.

In *dicta*, Justice Boyd said, "We have no problem holding that the exception applies to *all* Texas employers, …" private and governmental alike, but he refused to further hold that applying *Sabine Pilot* to a governmental entity also waived immunity from a wrongful termination suit. Waiver of immunity is a matter of legislative, not judicial, prerogative.

The court applied the same analysis to the prosecutor's argument that the Michael Morton Act embodied in Texas Code of Criminal Procedure §39.14 statutorily waived immunity. §39.14 obligates prosecutors to disclose exculpatory information, but says nothing about waiving immunity from suit. To accomplish that result, the statute must say so in "clear and unambiguous language."

Anticipating the court's deference to the legislature, the prosecutor also argued that the court should simply abolish governmental immunity from suit either entirely or for the limited purpose of implementing an exception for unlawful conduct. Although the court defers to the legislature for waivers of immunity where it exists, the judiciary "retains the authority and responsibility to determine whether immunity exists in the first place, and to define its scope." The opinion cites the examples of *Reata Constr. Corp. v. City of Dallas*, 197 S.W.3d 371, 374 (Tex. 2006), and *State ex rel. Best v. Harper*, 562 S.W.3d 1 (Tex. 2018), in which the refusal to recognize immunity from suit was based on the fact that both situations involved a governmental decision to get involved in litigation and thereby decided to expose itself to potential liability on a compulsory counterclaim or claim for an opponent's attorney's fees. This case did not involve a voluntary undertaking of the risks attendant to litigation. For this reason and the untenable resulting danger of unpredictable losses to the public treasury, the court declined to imply a waiver of immunity due to the *Sabine Pilot* exception.

Sovereign immunity does not apply when the suit is for conduct that is outside the scope of the state's authority – i.e., *ultra vires.* The court declined to consider the suggestion of *amici* that the wrongful termination case be

considered as a suit for *ultra vires* acts. It justified this refusal because the plaintiff prosecutor had taken the position throughout the case that the *Sabine Pilot* created a tort action for damages, not just an action for equitable relief.

Justice Guzman, joined by Justices Lehrmann and Devine, issued a concurring opinion calling on the Texas Legislature to strengthen statutory incentives to encourage disclosure of exculpatory evidence and punish its concealment.

***Employment Law*; *Contractual Disclaimers***: **Employee manual held not to be an employment contract for purposes of waiving sovereign immunity where the manual disclaimed that it was part of any employment contract.**

The court also gave credence to a disclaimer of the formation of any contract at all in *City of Denton v. Rushing, et al.* In that case, the dispute was over whether the City's Policy and Procedures Manual was a unilateral contract for purposes of §271.151 with respect to "on-call" time.

As mentioned in the previous *Update*'s discussion of *Rosenberg Development Corp. v. Imperial Performing Arts, Inc.*, under Texas Local Government Code §271.152, a governmental entity waives its immunity from suit on certain contractual obligations if entered with authority. Local Government Code §271.152 waives immunity if the contract is (1) a written statement (2) of an agreement's essential terms (3) for providing goods or services (4) to a local governmental entity (5) executed on behalf of that entity. Tex. Loc. Gov't Code §271.151(2)(A).

Before 2013, it was City policy that "on call" time was uncompensated. In 2013, the City Manager drafted a compensation policy that was approved by the City's Executive Committee, but never adopted by the City Council. These policies were nevertheless incorporated in the City's policies and procedure manual. The manual stated specifically that it was no part of the "the terms of a contract of employment." Several employees sued to recover compensation for past "on call" time under the revised "on call" pay policy.

According to a unanimous opinion by Justice Devine, the disclaimer in the manual was sufficient to prevent the "on call" provisions from being any part of an employment contract. The court, therefore, ordered dismissal of the employee's suit for want of jurisdiction due to the City's immunity.

The opinion rejected the reasoning of the court of appeals that the purpose of the disclaimer was only to preserve at-will employment status. The court "need not look any further" than the disclaimer itself to conclude that it effectively negated any intent for the policies and procedures manual to be a contract. Accordingly, §271.151's requirements for a waiver of immunity from suit were not satisfied. The court dismissed the employees' suit for want of jurisdiction.

***Governmental Immunity from Suit*: A municipality's contractual agreement incidental to a bridge restoration and development program was part of its governmental functions, but the waiver of immunity for breaches of such authorized contracts applied when the suit only sought equitable, not legal remedies.**

***Mootness, Waiver by Acquiescing in the Judgment*: A case remains a live controversy when the parties continue to dispute whether the action taken by the judgment obligor is sufficient to satisfy the judgment's requirements.**

***Appellate Procedure*: Although the court prefers to decide cases on substance rather than procedure, it signals that a litigant disregards the formalities of an affidavit at its peril when the affidavit is the only basis for proving necessary facts.**

In *Hays Street Bridge Restoration Group v. City of San Antonio*, Chief Justice Hecht wrote a unanimous opinion that the Local Government Contract Claims Act ("LGCCA") in Texas Local Gov't Code §§271.151-.160 waived governmental immunity in suits where the requested remedy is limited specific performance. The restoration group entered a written agreement that the City would dedicate to a bridge restoration project funds the group raised and donated to the City for the project. The group then arranged to have private owners donate property adjacent to the bridge for use as a park. After the restoration of the bridge was complete, the City changed its mind about creating a

park and – surprise! – sold the land for private development as a combination microbrewery, restaurant and event space.

The restoration group sued the City for specific performance of the City's promise to dedicate the donated "funds" to the restoration project. According to the group, the donated property was "funds" for purposes of the City's promise. Granting the group the requested specific performance, the trial court ordered the City to apply the property to the restoration project.

The City appealed, automatically staying the trial court's order. The restoration group moved to hold the City in contempt when it sought to proceed with the sale of the donated property. The City claimed that it honored its agreement because it had passed an ordinance that would apply proceeds from the sale of the donated property to the restoration project.

Before reaching the question of whether the LGCCA waived immunity for non-monetary relief, the opinion first addressed whether the case had become moot because of the City ordinance dedicating the sales proceeds from the donated property to funds for the restoration project. According to the City, this arrangement voluntarily satisfied the trial court's judgment and thereby mooted the appeal.

The opinion noted with annoyance that the City either: 1) prosecuted an appeal for which there was no jurisdiction, or 2) "lacked confidence" in its belated assertion that the case was moot. Ordinarily, the court prefers to overlook technical defects, but in this case it overruled the City's assertion that the case was moot in part because the declaration supporting the motion omitted the jurat. However, the court also explained that the case was not moot because the fundamental dispute remained: did the agreement apply to the property *in kind* or was it limitation to "funds" raised by the group only applicable to money so that the City complied with the agreement by selling the property and applying the proceeds of the sale to the project.

Turning to the immunity question, the opinion echoes the refrain from *Hillman* discussed above: the court decides whether immunity exists; the legislature decides whether to waive it. That this suit was for specific performance rather than money damages did not preclude immunity. There are only two classes of litigation in which a governmental entity is categorically vulnerable to suit: those alleging that a government official has acted *ultra vires* – i.e., exceeded the limits of the authority of the office – and those arising out of proprietary functions – functions that are only possible for a municipality to engage in. Immunity in this case rises or falls with whether the City was engaged in a proprietary function when it entered the agreement with the restoration group.

Under the in the *Wasson Interests* decisions from the two preceding terms, the proprietary-governmental divide is determined by the nature of the contractual undertaking, not the breach. Deciding the "nature" of a contract is guided first by consideration of the delineation of governmental and proprietary activities in §101.0215 of the Tort Claims Act and its general definitions of "governmental" and "proprietary" functions. The court concluded that the agreement in this case was properly considered governmental because it involved bridge maintenance and community development, both of which are statutorily designated as "governmental" functions. Moreover, the project was a benefit, not just to residents of the municipality, but to the public at large, which reinforces its character as governmental instead of proprietary.

Next, the court considered whether the City's immunity had been waived by Local Government Code §271.152. That waiver is limited by the next section of the Local Government Code, which restricts the amount of damages that can be recovered in a contract suit against a governmental entity. The court rejected the suggestion that the restriction of the limitation to monetary damages meant, by negative implication, that immunity for suits for equitable remedies such as specific performance had not been waived. The court ruled that the waiver granted in §271.152 "for a claim for breach of [a] contract" that a local governmental entity enters with statutory or constitutional authority was broad enough to waive immunity for a specific performance suit and the suit for that relief against the City was within the trial court's subject-matter jurisdiction.