

IN THE SUPREME COURT OF TEXAS

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No. 04-1003
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ARTURO FLORES, ET AL., APPELLANTS,

v.

MILLENNIUM INTERESTS, LTD., ET AL., APPELLEES

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ON CERTIFIED QUESTIONS FROM THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT
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Argued February 15, 2005

JUSTICE MEDINA delivered the opinion of the Court joined by JUSTICE HECHT, JUSTICE O'NEILL, JUSTICE WAINWRIGHT, JUSTICE JOHNSON, and JUSTICE WILLETT.

JUSTICE WAINWRIGHT filed a concurring opinion.

JUSTICE BRISTER filed a dissenting opinion joined by CHIEF JUSTICE JEFFERSON and JUSTICE GREEN.

This case comes to us on certified questions from the United States Court of Appeals for the Fifth Circuit asking us to construe section 5.077 of the Texas Property Code. That section requires that the seller of real property under an executory contract provide the buyer with an annual accounting statement and imposes "liquidated damages" should the seller fail to comply. The Fifth Circuit has asked the following questions about this statute:

1. If a seller under a contract for deed sends a purchaser a statement under § 5.077(a) that omits any of the applicable information listed in § 5.077(b) of the Texas Property Code, specifically in the information required by § 5.077(b)(1) or (3), or both, is the seller liable to the purchaser for \$250 per day liquidated damages as set forth in §

5.077(c)?

2. If a seller under a contract for deed sends a purchaser a statement that omits information required by §§ 5.077(b)(1) and (3), must the purchaser prove actual harm or injury to recover liquidated damages under the statute?

3. In 2001, 2002, and 2003, did the statutorily defined “exemplary damages” in chapter 41 of the Texas Civil Practice and Remedies Code encompass the statutorily defined “liquidated damages” in § 5.077 of the Texas Property Code, so that to recover under § 5.077 of the Property Code a purchaser would have to comply with § 41.003 of the Civil Practice and Remedies Code?

390 F.3d 374, 376-77 (5th Cir. 2004) (per curiam). The Fifth Circuit has further disclaimed “any intention or desire” that we “confine [our] reply to the precise form or scope of the questions certified.” *Id.* at 377.

We conclude that the annual statements in this case were timely under section 5.077(a) and that the omission of some information required by section 5.077(b) did not render them deficient or otherwise invoke the liquidated damages provision of section 5.077(c). We further conclude that the Legislature intended for the “liquidated damages” of section 5.077(c) to be a penalty and did not intend that a purchaser prove actual damages as a predicate to their recovery. We accordingly answer the first two questions posed by the Fifth Circuit, No, and conclude that those answers make it unnecessary to reach the third and final question.

I

Millennium Interests, Ltd. develops residential subdivisions in the Houston area, financing most of its sales either with traditional mortgages or executory contracts, also known as contracts for deed. A contract for deed, unlike a mortgage, allows the seller to retain title to the property until the purchaser has paid for the property in full. Such sales are regulated by statute which, among

other things, requires that the seller provide the purchaser with an annual accounting statement on or before January 31 each year. *See* TEX. PROP. CODE § 5.077. If the seller fails to send the statement on time, the statute makes the seller liable to the purchaser for “liquidated damages” and attorney’s fees. *Id.* § 5.077 (c).

The purchaser’s statutory right to liquidated damages and attorney’s fees under a contract for deed is relatively new, added in 2001, when the Legislature renumbered and revised the statutes applicable to such contracts.¹ Previously, the statute had allowed the purchaser to deduct 15% of his or her monthly payments beginning on the date on which the required information was demanded until the date on which it was provided.² The 2001 amendments, however, changed this to provide:

(c) A seller who fails to comply with subsection (a) is liable to the purchaser for:

(1) liquidated damages in the amount of \$250 a day for each day after January 31 that the seller fails to provide the purchaser with the statement; and

(2) reasonable attorney’s fees.

¹ The 2001 amendments made the reporting requirement and other provisions regarding executory contracts applicable to Millennium’s properties in Harris County. Those provisions previously had been applicable only in counties that the Texas Department of Housing and Community Affairs had determined were within 200 miles of an international border and had a below-average per capita income and an above average unemployment rate. *See* Act of June 17, 1995, 74th Leg., R.S. Ch. 994, § 3, 1995 Tex. Gen. Laws 4983-84 (formerly TEX. PROP. CODE § 5.091), *amended by* Act of June 13, 2001, 77th Leg., R.S. Ch. 693, § 1, 2001 Tex. Gen. Laws 1319 (current version at TEX. PROP. CODE § 5.062); SENATE COMMS. ON INT’L RELATIONS, TRADE TECH., BILL ANALYSIS, Tex. S.B. 336, 74th Leg., R.S. (1995); *see also De La Cruz v. Brown*, 109 S.W.3d 73,76 (Tex. App.–El Paso 2003), *rev’d on other grounds*, 156 S.W.3d 560 (Tex. 2004).

² Act of June 17, 1995, 74th Leg., R.S. Ch. 994, § 3, 1995 Tex. Gen. Laws 4987 (formerly TEX. PROP. CODE § 5.100), *amended by* Act of June 13, 2001, 77th Leg., R.S. Ch. 693, § 1, 2001 Tex. Gen. Laws 1326-27 (current version at TEX. PROP. CODE § 5.077).

TEX. PROP. CODE § 5.077(c). These “liquidated damages” are triggered by the seller’s failure to comply with subsection (a), which provides:

(a) The seller shall provide the purchaser with an annual statement in January of each year for the term of the executory contract. If the seller mails the statement to the purchaser, the statement must be postmarked not later than January 31.

Id. § 5.077(a). Subsection (b) then lists the information that must be provided in the annual statement, which includes:

- (1) the amount paid under the contract;
- (2) the remaining amount owed under the contract;
- (3) the number of payments remaining under the contract;
- (4) the amounts paid to taxing authorities on the purchaser’s behalf if collected by the seller;
- (5) the amounts paid to insure the property on the purchaser’s behalf if collected by the seller;
- (6) if the property has been damaged and the seller has received insurance proceeds, an accounting of the proceeds applied to the property; and
- (7) if the seller has changed insurance coverage, a legible copy of the current policy, binder or other evidence that satisfies the requirements of Section 5.070(a)(2).

Id. § 5.077(b).

In July 2000, Millennium retained Concord Servicing Corp. to perform accounting and reporting services for its financing transactions. Concord provided two annual statements to each of Millennium's customers, an “Annual Interest Statement” and an “Escrow Analysis.” Unfortunately, these statements failed to include two items required by the statute, the “amount paid

under the contract” and “the number of payments remaining under the contract.”³ *Id.* § 5.007(b)(1), (3).

Consequently, three purchasers sued Millennium for these omissions in their 2001 and 2002 annual statements, seeking statutory damages. At the summary judgment hearing in May 2003, these purchasers claimed that they were entitled to statutory damages greatly in excess of the purchase prices of their respective properties. The federal district court disagreed, however, rendering summary judgment for Millennium. The court concluded that:

- Millennium had timely provided annual statements to the purchasers;
- Section 5.077(c) permits the recovery of liquidated damages of \$250 per day only for violation of Section 5.077(a), which requires the timely mailing of annual statements to purchasers under a contract for deed;
- Section 5.077(c) does not similarly provide for liquidated damages for violation of Section 5.077(b), which delineates the contents of an annual statement; and
- Because Section 5.077(c) does not provide for liquidated damages when a statement is timely provided, the plaintiffs were not entitled to recover in the absence of proof of actual damages.

273 F. Supp. 2d 899, 901. The purchasers appealed the summary judgment in Millennium’s favor to the Fifth Circuit, which certified the aforementioned questions to us.

II

The first certified question asks whether section 5.077(c)’s liquidated damages are owed when a seller delivers a timely annual statement that omits some of the information listed in subsection (b) of that statute. The plain wording of the statute is argued in support of conflicting

³ The annual statements also did not include the last three items relating to insurance, which is understandable because Millennium neither provided, received, nor changed insurance on these properties.

interpretations. The purchasers argue that because subsection (b) defines what information an “annual statement” must include, a document that does not contain this information cannot be an annual statement. Thus, the purchasers conclude that statutory damages apply until they receive a complete annual statement, incorporating all of the information required by subsection (b). Millennium argues, on the other hand, that because the statute plainly premises statutory damages only upon the seller’s failure to provide the purchaser with a timely annual statement, subsection (a), without mentioning subsection (b), that a timely annual statement may omit some of the information required by subsection (b) and not invoke the liquidated damages provision. Millennium further submits that had the Legislature intended otherwise, it would have conditioned the assessment of liquidated damages upon the seller’s failure to comply with both subsections (a) and (b) of the statute.

The parties also disagree about the nature of these statutory damages. Millennium argues that these damages are penal in nature because they bear no relation to a purchaser’s actual damages when receiving a late annual statement. The purchasers respond that the Legislature did not intend for them to be a penalty because it labeled the recovery as “liquidated damages.”

The term “liquidated damages” ordinarily refers to an acceptable measure of damages that parties stipulate in advance will be assessed in the event of a contract breach. *Valence v. Dorsett Operating Co.*, 164 S.W.3d 656, 664 (Tex. 2005). The common law and the Uniform Commercial Code have long recognized a distinction between liquidated damages and penalties. *See Stewart v. Basey*, 245 S.W.2d 484, 485-486 (Tex. 1952); TEX. BUS. & COM. CODE § 2.718(a). If damages for the prospective breach of a contract are difficult to measure and the stipulated damages are a

reasonable estimate of actual damages, then such a provision is valid and enforceable as “liquidated damages;” otherwise it is void as a “penalty.” *Phillips v. Phillips*, 820 S.W.2d 785, 788 (Tex. 1991). The purchasers therefore conclude that these damages cannot be both “liquidated damages” and a “penalty.”

While we agree that this is true at common law, it does not always hold true for statutes. Aside from the 2001 amendments to the Property Code,⁴ twelve Texas statutes mention liquidated damages, nine of which involve the regulation of liquidated damage provisions in contracts.⁵ Representative here is section 2.718 of the Business & Commerce Code which codifies the common law distinction as part of Texas’ adoption of the Uniform Commercial Code’s article on sales.⁶ The Legislature, however, has also used the term “liquidated damages” in other contexts and, on

⁴ In addition to section 5.077(c), at issue in this lawsuit, which assesses “liquidated damages” in connection with the requirement that the seller submit an annual accounting statement, section 5.079(c) assesses “liquidated damages” in connection with the requirement that the seller submit a deed upon payment of the contract.

⁵ See TEX. AGRIC. CODE § 52.016(d)(1) (a marketing association may “fix as liquidated damages specific amounts to be paid by a member if the member breaches the marketing contract”); TEX. BUS. & COM. CODE § 2.718 (codifying common law treatment of liquidated damages as part of UCC); TEX. BUS. & COM. CODE § 2A.103(a)(7)(iii) (in finance lease, lessee must receive statement describing any liquidated damages provided to the lessor by the person supplying the goods); TEX. BUS. & COM. CODE § 2A.503(c) (permitting liquidated damages in lease agreement); TEX. CIV. PRAC. & REM. CODE § 141.003(7) (in structured settlement, statement provided to payee must show “the amount of any penalties or liquidated damages payable by the payee in the event of any breach of the transfer agreement by the payee”); TEX. GOV’T CODE § 466.102 (state lottery commission must provide in contracts for “liquidated damages and a performance bond in an amount equal to the executive director’s best estimate of the revenue that would be lost if the contractor fails to meet deadlines specified in the contract”); TEX. LOCAL GOV’T CODE § 116.023(b) (if bank chosen as county depository fails to provide bond, county will retain application fee as liquidated damages); TEX. LOCAL GOV’T CODE § 117.021(c) (if bank chosen as special fund county depository fails to provide bond, county will retain application fee as liquidated damages); TEX. TRANSP. CODE § 223.012(a)(1) (state highway department to “develop a schedule for liquidated damages that accurately reflects the costs associated with project completion delays”).

⁶ “Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or non-feasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty.” TEX. BUS. & COM. CODE § 2.718(a).

occasion, has used it when referring to a penalty.⁷ For example, section 62.201 of the Labor Code imposes a civil penalty against an employer who violates minimum wage laws in the amount of “the unpaid wages plus an additional equal amount as liquidated damages.” Article 6362 of the revised civil statutes imposes a penalty of “five hundred dollars as liquidated damages” payable to the shipper if a railroad charges more for a double-decked carload of sheep than for a similar shipment of cattle, but also waives “the penalties prescribed in this article” under certain circumstances.

In 2001, the Legislature amended the Property Code to add, among other things, two provisions for “liquidated damages,” the provision at issue here, section 5.077(c), and section 5.079(c). This latter section assesses “liquidated damages” against a seller who fails to promptly tender a deed within 30 days after the purchaser’s final payment under a contract for deed. The predecessor to section 5.079(c) imposed a “penalty” upon a seller for this same conduct, setting the penalty at \$250 per day for the first 90 days and \$500 per day for each day thereafter. *See* Act of June 17, 1995, 74th Leg., R.S. Ch. 994, § 3, 1995 Tex. Gen. Laws 4988 (formerly TEX. PROP. CODE § 5.102), *amended by* Act of June 13, 2001, 77th Leg., R.S. Ch. 693, § 1, 2001 Tex. Gen. Laws 1327 (current version at TEX. PROP. CODE § 5.079). The 2001 amendment recharacterized these penalties as “liquidated damages” but did not otherwise change the statutory formula for computing these damages. *See id.*

⁷ *See* TEX. LABOR CODE § 62.201 (imposing civil penalty against employer violating minimum wage laws); TEX. REV. CIV. STAT. art. 6362 (imposing civil penalty on railroad for freight overcharges); TEX. CODE CRIM. PROC. art. 18.20 § 16(a) (providing for the recovery of actual and punitive damages for violation of wiretapping laws “but not less than liquidated damages computed at a rate of \$100 a day for each day of violation or \$1000, whichever is higher”).

In *Brown v. De La Cruz*, 156 S.W.3d 560 (Tex. 2004), we compared section 5.079(c) to its predecessor to aid our understanding of whether the earlier version provided a private right of action for these penalties. We held that it did not, observing that “by changing ‘penalty’ to ‘liquidated damages’ and adding a provision for attorney’s fees, the Legislature changed not just the recipient but the nature of the amounts assessed.” *Id.* at 565. Thus, we concluded that the 2001 amendment had created a private right of action for these statutory damages – a right that could not be inferred from the language of the original statute. *Id.* We did not decide, however, whether the assessment of “liquidated damages” in section 5.079(c) was compensatory or penal in nature, although we did note, in passing, that the severity of the statutory formula “would in many instances impose a fine far beyond the damages that a purchaser is likely to suffer.” *Id.* at 566.

This observation from *Brown* is instructive here because sections 5.079(c) and 5.077(c) share a similar statutory formula for computing liquidated damages. According to Millennium’s math, that formula yields liquidated damages in this case in excess of five times the value of the underlying properties. Such an award obviously bears no relation to the harm caused by a late or incomplete annual statement; in fact, these purchasers candidly admit that they have not been harmed.

We have found statutory damage schemes far less draconian than this one to be penal in nature. See *Johnson v. Rolls*, 79 S.W. 513, 514 (Tex. 1904) (statutory liquidated damages awarded without reference to any actual loss or injury have “much the character of exemplary or punitive damages”); *The Houston & Tex. Central Ry. Co. v. H.W. Harry & Bros.*, 63 Tex. 256, 260 (1885)(to the extent that an award of statutory damage exceeds the amount necessary to compensate plaintiff’s injury, “the excess is but exemplary damage”). In fact, before the 2001 amendments, there was little

doubt that the Legislature also thought of these damages as a penalty. At least that is how section 5.079(c)'s predecessor referred to them. *See Brown*, 156 S.W.2d at 563 (quoting former § 5.102(b) of the Property Code). Merely changing the label for these statutory damages did not, without more, change their underlying character; they remain penal in nature.

As a penal statute, section 5.077 must be strictly construed. *See id.* at 565 (“statute providing for a daily penalty unrelated to actual losses must be strictly construed”). The statute conditions liability for “liquidated damages” on the seller’s failure to provide an annual statement by the statutory deadline. And although the statute also lists the information that must be included in that statement, it does not, strictly speaking, trigger an award of “liquidated damages” when some of that information is missing. By tying the statutory penalty to timely delivery of the annual statement, but not its contents, the Legislature’s apparent purpose was to provide the purchaser with certain annual information about the parties’ executory contract and to incite further inquiry if some of that information was missing or incomplete. Accordingly, we conclude that an annual statement under Section 5.077 that omits some required information does not invoke the “liquidated damages” provision unless the statement is so deficient as to be something other than a good faith attempt by the seller to inform the purchaser of the current status of their contractual relationship. The answer to the first certified question is, therefore, No.

The company hired by Millennium to service its financial transactions was apparently unaware of recently enacted disclosure requirements specifically applicable to executory contracts and accordingly sent these purchasers the same statements it typically used to service traditional mortgage loans. Those statements disclosed two of four items of information required by section

5.077(b),⁸ the “remaining amount owed on the contract” and the “amounts paid to taxing authorities.” TEX. PROP. CODE § 5.077(b)(2), (4). It also disclosed part of another item, providing the amount of interest paid during the prior year, but did not state the total “amount paid under the contract,” or the “number of payments remaining under the contract.” *Id.* § 5.077(b)(1), (3). These omissions, while significant, do not demonstrate such a blatant attempt to circumvent the disclosure requirements as to render the annual statement a nullity.

III

The Fifth Circuit next asks whether a purchaser must prove actual harm or injury to recover statutory damages for an incomplete annual statement. We find nothing in the statute to suggest such a requirement. Moreover, to conclude that actual damages are a predicate to recovery under this statute would belie our conclusion that the liquidated damages provision is, in fact, punitive rather than compensatory. Accordingly, our answer to the second question certified is also, No.

Finally, the Fifth Circuit asks whether the “liquidated damages” imposed under this statute are also “exemplary damages” under Chapter 41 of the Texas Civil Practice and Remedies Code, such that a purchaser must also comply with the requirements of Chapter 41 to collect these statutory damages. Chapter 41 generally limits the award of exemplary damages, which it broadly defines as any damages that are “awarded as a penalty or by way of punishment.” TEX. CIV. PRAC. & REM. CODE § 41.001(5).⁹ Because the incomplete annual statement here did not invoke the liquidated

⁸ The statute actually lists seven items of required information, but the last three, relating to insurance coverage, are not applicable in this case. *See* n.3, *infra*.

⁹ This provision was amended in 2003 to define “exemplary damages” as “any damages awarded as a penalty or by way of punishment *but not for compensatory purposes*.” (Emphasis added).

damages provision of Section 5.077(c), we decline to decide at this time whether these statutory damages are also “exemplary damages” within the meaning of Chapter 41.

* * * * *

In summary, we conclude that an annual statement that omits some of the information required by Section 5.077(b) does not invoke “liquidated damages” under Section 5.077(c) unless the statement is so deficient as to be something other than a good faith attempt by the seller to inform the purchaser of the current status of their contractual relationship. We further conclude that these statutory damages are penal in nature and do not require actual harm as a predicate to recovery.

Justice David M. Medina

Opinion delivered: September 30, 2005