Discovery Sharing in Texas: Litigant Confidentiality v. Litigation Costs

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I. INTRODUCTION

Texas courts have long allowed discovery sharing between similar cases.1 Discovery sharing has a multitude of systemic benefits—not the least of which is reducing pretrial litigation costs.2 Despite these

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1See Garcia v. Peeples, 734 S.W.2d 343, 348 (Tex. 1987).

2See, e.g., Dustin B. Benham, Proportionality, Pretrial Confidentiality, and Discovery Sharing, 71 WASH. & LEE L. REV. 2181, 2229 (2014) (describing the efficiencies of discovery sharing); see also MANUAL FOR COMPLEX LITIGATION (FOURTH) § 11.432 (2004) (endorsing sharing).
advantages, some contend that the Supreme Court of Texas should forbid the practice in cases involving trade secrets. But the court should not limit discovery sharing—doing so would run contrary to Texas’s efforts to reduce undue litigation expenses.

Discovery sharing is prevalent in product-liability cases involving nationally distributed products. Indeed, recent media coverage of the GM defective-ignition crisis (and GM’s surprising simultaneous attack on sharing at the supreme court) has highlighted the war over discovery sharing in Texas. Sharing’s widespread use in products cases is not surprising: identical products (if defective) tend to injure people similarly across the products’ distribution area. Attorneys representing those injured people tend to be interested in similar information across cases—the product design, design and manufacturing processes, safer alternative designs, and information surrounding the manufacturing company’s knowledge of the defect.

Discovery sharing allows these attorneys, representing people with similar claims against common or related defendants, to avoid reinventing the wheel. Put simply, attorneys and parties in a sharing system reuse the
discovery information obtained in previous cases to avoid wasteful rediscovery.

Someone not familiar with the issue might wonder, “What could possibly be wrong with sharing information between similar cases? Isn’t that commonsense?” But despite its somewhat obvious appeal as a cost-saving measure, discovery sharing often runs head on into another important interest in pretrial discovery: the protection of proprietary information.9

Litigants routinely ask courts to enter orders to limit the dissemination of competitively sensitive discovery information (like product designs).10 They putatively do so, at least in part, to keep the information from competitors.

Sharing proceeds on the theory that the practice does not hamper the competitive value of discovery information shared only among non-competitor litigants.11 If the audience for discovery information is limited to similar litigants, the reasoning goes, the value of the proprietary or trade secret information remains intact.12

But those who oppose sharing contend otherwise—sharing trade secrets, even among non-competitors, increases the risk of inadvertent or intentional disclosure to competitors by sharing attorneys and litigants.13 Moreover, according to some of these voices, sharing violates Texas’s qualified trade secret privilege by allowing collateral litigants to receive information without demonstrating that the information is necessary in their particular cases.14

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9 See Garcia v. Peeples, 734 S.W.2d 343, 345–47 (Tex. 1987) (balancing trade secret holder’s interest against the “public policies favoring the exchange of information”); see also, e.g., Richard P. Campbell, The Protective Order in Products Liability Litigation: Safeguard or Misnomer?, 31 B.C. L. Rev. 771, 824–25 (1990) (opposing discovery sharing for, among other reasons, its potential to undermine the value of proprietary information).


11 See, e.g., Garcia, 734 S.W.2d at 348 (holding that trial court should have balanced competing needs for information by sharing litigants against producing party’s interest in preventing dissemination to competitors).

12 See id.

13 See, e.g., Campbell, supra note 9, at 824–25 (contending that discovery sharing increases risk of disclosure of competitively sensitive information).

This Article is the first piece of scholarship to evaluate these arguments in light of historic and recent efforts to make Texas and federal pretrial procedure more efficient. After evaluating both pro- and anti-sharing positions, the Article concludes that sharing furthers pretrial efficiency without unduly compromising trade secret and other confidential information.

The Article proceeds in four parts. First, it examines the development of discovery sharing as a routine practice. Second, the Article considers some common arguments against discovery sharing. Third, it briefly examines the relationship between sharing and efforts to reduce pretrial costs, both in the Texas and federal court systems. Finally, the Article contends that sharing is a practice that both reduces costs and is compatible with litigants' proprietary-information interests, even in cases involving trade secrets.

II. THE DEVELOPMENT OF DISCOVERY SHARING

The story of discovery sharing and the story of protecting trade secrets in discovery have been intertwined from the beginning. This entanglement comes from a practical reality in product-liability cases: parties simultaneously allege that the design of the product is both dangerous and a trade secret. Indeed, plaintiffs seeking to prove that a dangerous product caused injury send over volleys of discovery requests for the product’s design as proof of its danger. The party resisting these requests (typically the defendant) often contends that the product’s design is a privileged trade secret.

15See, e.g., Garcia, 734 S.W.2d at 344-45, 348 (entering non-sharing protective order was abuse of discretion in a trade secret case); cf. also, e.g., Laurie Kratky Doré, Secrecy by Consent: The Use and Limits of Confidentiality in the Pursuit of Settlement, 74 NOTRE DAME L. REV. 283, 364-65 (1999) (recognizing that “injury to a cognizable privacy or property interest” can weigh against discovery sharing).

16In another typical version, a corporate defendant alleges that its practices constitute trade secrets while a plaintiff alleges that those same practices were injurious. See, e.g., Endicott, 81 So. 3d at 488.

17See, e.g., Raymond Handling Concepts Corp. v. Superior Court, 45 Cal. Rptr. 2d 885, 885-86 (Cal. Ct. App. 1995) (assessing protective order in case involving designs of an allegedly injurious forklift); Garcia, 734 S.W.2d at 344-45.

18See, e.g., Garcia, 734 S.W.2d at 344-46.
Courts and litigants facing this fight often compromise. Instead of denying discovery of product designs (undoubtedly vital proof in many products cases), courts typically allow discovery of the information subject to a "protective order." These protective orders vary in their particulars, but in general they limit the audience for the discovery information at stake to something less than the general public. For instance, a protective order might restrict discovery access to just the parties and attorneys in the particular case (a "non-sharing" protective order). In contrast, a more lenient order might allow access for individuals in similar cases (a "sharing" protective order).

Note that in both versions, the protective orders' audience limitation implicitly excludes product-producing competitors (who are corporations that will almost certainly not be injured physically by a competing product and therefore are unlikely to be "similar" litigants). And many protective orders exclude competitors with language that expressly declares that discovery information shall not be shared with competitors, even if they are in similar litigation.

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19 See, e.g., United Nuclear Corp. v. Cranford Ins. Co., 905 F.2d 1424, 1427 (10th Cir. 1990) (recognizing that stipulated protective orders are common).

20 Id. But see, e.g., In re Bass, 113 S.W.3d 735, 745–46 (Tex. 2003) (denying discovery of trade secret information where party failed to establish that the information was necessary proof in case); In re Cont'l Gen. Tire, Inc., 979 S.W.2d 609, 615 (Tex. 1998) (same).

21 See FED. R. CIV. P. 26(c)(1)(G) (allowing courts to limit the audience for discovery materials); TEX. R. CIV. P. 192.6 (same).


23 See, e.g., Raymond Handling Concepts Corp. v. Superior Court, 45 Cal. Rptr. 2d 885, 886 (Cal. Ct. App. 1995) (upholding a trial court's protective order providing that "plaintiffs counsel may disclose said discovery so designated as confidential to counsel in other pending similar litigation").

24 Cf. Pincheira v. Allstate Ins. Co., 190 P.3d 322, 337 (N.M. 2008) (noting that "sharing among other litigants and witnesses" is often appropriate where those sharing the information "are not competitors of the [producing] defendant").

25 See, e.g., Garcia v. Peeples, 734 S.W.2d 343, 348 (Tex. 1987) ("Out of an abundance of caution, the trial court, after determining which documents are true trade secrets, can require those wishing to share the discovered material to certify that they will not release it to competitors or others who would exploit it for their own economic gain.").
By excluding competitors, these orders protect the value of product-design information. Indeed, trade secrets are valuable precisely because they are secret from a particular group—competitors who would make use of the information to gain an undue advantage in the marketplace.

So, for instance, imagine that a company spends millions to design a product and keeps its efforts secret. If a competing company gained access to the information, it would have the benefit of the first company's research and development without spending substantial resources. This windfall would simultaneously devalue the design for the first company because it would now potentially compete, on equal or similar design footing, with the company that obtained the design. Presumably, competition between the two would cause the price of the product to fall, reducing the first company's profits.

This hypothetical highlights the theory behind audience-limiting protective orders—not all audiences are created equal. An injured individual who seeks a product design for use in a lawsuit does not have the capability (or likely the interest) to use the information to build the product and compete in the marketplace against a product manufacturer. And so long as that individual is ordered not to disclose the information to such competitors, a court order to turn over the information in discovery does not injure the product-producing company.

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26 See, e.g., Jampole v. Touchy, 673 S.W.2d 569, 574 (Tex. 1984) (holding that trial court abused its discretion by denying discovery of product information where protective order keeping information from competitors would have sufficiently protected manufacturer's interest).

27 See, e.g., Ruckelshaus v. Monsanto Co., 467 U.S. 986, 1011 n.15 (1984) ("We emphasize that the value of a trade secret lies in the competitive advantage it gives its owner over competitors."); cf. also RESTATEMENT (FIRST) OF TORTS § 757 cmt. b (AM. LAW INST. 1939) ("A trade secret may consist of any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it.").

28 See RESTATEMENT (THIRD) OF UNFAIR COMPETITION § 39 (AM. LAW INST. 1995) ("[T]he protection of trade secrets has been justified as a means to encourage investment in research by providing an opportunity to capture the returns from successful innovations.").

29 See, e.g., Garcia, 734 S.W.2d at 348 (noting that trade-secret-holder defendant's interest was in protecting proprietary product designs from competitors; plaintiff's interest was in effectively preparing for trial).

30 See, e.g., Jampole, 673 S.W.2d at 574 ("Jampole is not GMC's business competitor, and GMC acknowledged that, if the documents were relevant, any proprietary interest could be safeguarded by a protective order.").
The story gets more complicated, though, because many allegedly defective products injure many people who pursue lawsuits contemporaneously. Imagine that our product is a defective drug sold by a national company to treat a common condition.\textsuperscript{31} The history of pharmaceutical claims shows that when a nationally distributed drug purportedly causes injury, hundreds (if not thousands) of people file suit.\textsuperscript{32} In each of these suits, one core issue almost certainly will be whether the design of the drug is dangerous.\textsuperscript{33} Should the plaintiff in each suit be forced to litigate his or her entitlement to this design information? Should the courts be forced to resolve hundreds of identical discovery disputes?\textsuperscript{34}

These questions are particularly acute in light of what some have characterized as a discovery-cost crisis. According to these voices, the costs of discovery in U.S. litigation outweigh its benefits in many cases.\textsuperscript{35} Litigants and courts, the reasoning goes, are forced to expend resources to facilitate the discovery of information with scant connection to the merits of the case.\textsuperscript{36} And with the technological revolution of the past two decades,

\textsuperscript{31} The Yaz birth control lawsuit provides a real-world analogue—women across the country filed suit alleging that the drug injured them by creating blood clots, strokes, and heart attacks. See, e.g., 120 AM. JUR. Trials § 429 (2011) ("More than 50 women claim in lawsuits filed in Indianapolis that they suffered strokes, heart attacks or other serious health problems while taking the birth control pills Yasmin or Yaz, manufactured by Bayer Healthcare Corporation. Across the nation, dozens of lawsuits have been filed in the past few months by women claiming similar health problems after taking the pills.").

\textsuperscript{32} See id.

\textsuperscript{33} See, e.g., id. (woman brought products liability suit for defective design of a birth control patch).

\textsuperscript{34} See id. Many national-scale products suits, including the Yaz lawsuits mentioned above, end up in multidistrict litigation. Id. This trend has the effect of consolidating discovery for all cases subject to the MDL and presumably, reducing the need for informal discovery sharing. See id.

\textsuperscript{35} FED. R. CIV. P. 26(b)(1) (Advisory Committee’s note to 2015 proposed amendment) ("The 1983 Committee Note stated that [provisions limiting the breadth of discovery] were added ‘to deal with the problem of over-discovery.’ The objective is to guard against redundant or disproportionate discovery by giving the court authority to reduce the amount of discovery that may be directed to matters that are otherwise proper subjects of inquiry.’), cf. Richard Marcus, Procedural Postcard from America, 1 RUS. L.J. 9, 17 (2013) ("As a political matter, the notion that American litigation is too costly and time-consuming has gained much force. As an empirical matter, proving or evaluating such claims is difficult and involves contentious value judgments.”).

\textsuperscript{36} FED. R. CIV. P. 26(b)(1) (Advisory Committee’s note to 2015 proposed amendment).
the amount of all information subject to discovery (connected strongly to
the merits or not) has soared to terabytes in many cases.37

Over the years, in the federal and Texas systems, rule makers have
attempted to reign in discovery costs.38 Some commentators have
questioned the efficacy of their efforts.39 Whatever the merits of that debate,
recent amendments to the Federal Rules of Civil Procedure expressly target
the lack of “proportionality” between the costs of discovery and its
benefits.40 Those amendments are discussed in some depth in Part IV.B.

Outside of the recent discovery amendments, several procedural
innovations have sought to reduce litigation costs in repeating case
contexts, like product liability. For instance, multi-district litigation has
become prevalent over the past thirty years, allowing a single court to
resolve common issues in similar cases.41 But for similar cases not subject
to MDL, questions persist about the sanity of allowing multiple courts to
resolve virtually identical discovery issues.

Courts and litigants have grappled with informal solutions. Some courts
enter sharing protective orders to allow litigants to cooperate and share
information.42 Litigants have attempted to capitalize on sharing orders by

37 Cf., e.g., Dana A. Remus, The Uncertain Promise of Predictive Coding, 99 IOWA L. REV. 1691, 1696 (2014) (“The unmanageable scope and extent of e-discovery offered new opportunities for abuse and quickly became a principal cause of increasing costs and delays in the court system.”).

38 See, e.g., MCDONALD & CARLSON, supra note 4, § 13:2 (observing that 1999 amendments to the Texas Rules of Civil Procedure “were made to streamline discovery procedures and to reduce costs and delays associated with discovery practice”); Benham, supra note 2, at 2218-19 (chronicling federal efforts).

39 See Jordan M. Singer, Proportionality’s Cultural Foundation, 52 SANTA CLARA L. REV. 145, 148 (2012) (observing that attempts to reign in broad discovery have had “virtually no impact”).


41 See Martin H. Redish & Julie M. Karaba, One Size Doesn’t Fit All: Multidistrict Litigation, Due Process, and the Dangers of Procedural Collectivism, 95 B.U. L. REV. 109, 116 (2015) (“Since its inception in the late 1960s, MDL has become more and more common, to the point where today its use could almost be called routine.”).

creating information exchanges of varying levels of formality. These exchanges typically stockpile discovery information in repeating cases and allow members to access it for a fee, subject to the terms of applicable protective orders. Corporate defendants have resisted the sharing phenomenon, contending that shared discovery increases the risk of inadvertent or intentional disclosure of secret information to a competitor or the public at large.

In the mid-1980s, the Supreme Court of Texas stepped into the middle of this fight by enshrining sharing protective orders in Texas practice with its landmark decision, Garcia v. Peeples. Garcia was a paradigmatic case—an individual plaintiff alleged that the fuel system in a common General Motors vehicle was defective and caused a deadly fuel-fed fire. The plaintiff and his attorneys sought to share design information with litigants in similar lawsuits; GM contended that doing so would compromise its trade secrets.

But the story of trade secrets and discovery sharing in Texas did not begin and end with Garcia. Before the case, Texas courts had at least a partial framework for protecting trade secrets in discovery. And long after Garcia was decided, Texas courts continue to grapple with questions about

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43 See, e.g., Ward v. Ford Motor Co., 93 F.R.D. 579, 579 (D. Colo. 1982) ("Facing a single large manufacturer capable of coordinating its defenses nationwide, and a complex design engineering problem, about fifty attorneys representing the plaintiffs in many of these cases have organized an information exchange or clearing house for sharing information obtained by any of them through discovery.").

44 See Howard M. Erichson, Informal Aggregation: Procedural and Ethical Implications of Coordination Among Counsel in Related Lawsuits, 50 DUKE L.J. 381, 396 (2000) ("The Attorney's Information Exchange Group (AIEG), a nonprofit cooperative comprised of ATLA members representing plaintiffs in products liability cases, provides members with extensive discovery information. AIEG describes its primary objective: 'to provide plaintiffs' counsel with the same collaborative benefits that defense attorneys have long enjoyed.' AIEG information has been credited with aiding plaintiff victories against manufacturers of all-terrain vehicles and other products. One products liability lawyer called AIEG 'the first and least expensive step in evaluating [product] design.'").

45 Cf. Campbell, supra note 9, at 824-25 ("[T]he likelihood of [protective order] violation[s], inadvertent or otherwise, will increase in direct proportion to the number of disclosures.").

46 734 S.W.2d 343, 349 (Tex. 1987).

47 Id. at 344.

48 Id. at 344–45.

49 See infra, Part II.A.
sharing trade secrets and the more fundamental question of whether they are discoverable in the first place.  

A. Confidential Discovery

For more than fifty years, Texas has protected trade secrets in discovery, and the supreme court has routinely reiterated the importance of doing so. The trade secret privilege (which existed at common law) was enshrined in Texas Rule of Evidence 507 in 1983. This qualified privilege gives litigants grounds to refuse to produce trade secret information except in cases where not producing the information would work a fraud or injustice. Moreover, and as discussed in more depth in Part III, Rule 507

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50 See, e.g., In re Bass, 113 S.W.3d 735 (Tex. 2003); In re Cont’l Gen. Tire, Inc., 979 S.W.2d 609 (Tex. 1998).
51 See former TEX. R. CIV. P. 186(b) (West 1957, repealed 1984), replaced with the current protective-order rule, TEX. R. CIV. P. 192.6.
52 See, e.g., In re Bass, 113 S.W.3d at 739 (adopting a multi-factor test to protect trade secrets); In re Cont’l, 979 S.W.2d at 612 (Texas’s trade secret privilege “recognizes that trade secrets are an important property interest, worthy of protection.”); Garcia, 734 S.W.2d at 346 (noting that Texas courts have long observed the “importance” of protecting trade secrets); Lehnard v. Moore, 401 S.W.2d 232, 235 (Tex. 1966) (recognizing a qualified trade secret privilege).
53 See TEX. R. EVID. 507.
54 See id. Texas Rule of Evidence 507 mandates that trade secrets are privileged but fails to define what a “trade secret” is. Id. Courts in Texas have filled the gap. In 2003, the Supreme Court of Texas clarified the trade secret definition. In re Bass, 113 S.W.3d at 739. In Bass, the court recognized the Restatement of Torts’ six-factor test for determining whether information is a trade secret:

1. the extent to which the information is known outside of his business;
2. the extent to which it is known by employees and others involved in his business;
3. the extent of the measures taken by him to guard the secrecy of the information;
4. the value of the information to him and to his competitors;
5. the amount of effort or money expended by him in developing the information;
6. the ease or difficulty with which the information could be properly acquired or duplicated by others.

Id. The court went on to recognize that the Restatement (Second) of Torts did not include the trade secret definition. Id. Rather, the test was relocated to the Restatement (Third) of Unfair Competition. Id. That Restatement included the six-factor test in the reporter’s notes to section 39. Id. Those notes observe that the test is relevant in determining whether information is a trade secret, but the factors are not exclusive or dispositive. Id. The supreme court agreed, holding that a party seeking trade secret status for information need not demonstrate that all six of the restatement factors weigh in its favor. Id. at 740. Rather, courts may consider some or all of the factors in assessing whether information merits trade secret status. Id.
requires courts to provide “adequate” protection for trade secret information when litigants are forced to produce it.  

In this way, the Texas trade secret privilege dovetails with Texas Rule of Civil Procedure 192.6, the rule that gives courts rule-based authority to enter audience-limiting protective orders.  

This protective-order rule, like its federal counterpart, Rule 26(c), allows courts to mitigate the ill effects of what would be public disclosure of secret information in pretrial discovery.  

The Texas rule is silent on the burden to obtain such an order, but the supreme court has suggested that the federal “good cause” framework under Rule 26(c) is analogous.  

Federal law (and presumably consistent Texas law) requires parties seeking an audience-limiting order to make two showings. First, litigants must typically demonstrate that the information is in fact “confidential.” “Confidential information” is a broader category than “trade secrets” and sometimes includes secret, non-privileged commercial or personal information. Thus, the rule recognizes that much of the information exchanged in discovery will not meet the more onerous trade secret standard yet still be secret, sensitive, or private. The paradigm

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55 Tex. R. Evid. 507(c).  
58 See, e.g., Garcia v. Peeples, 734 S.W.2d 343, 345 n.1 (Tex. 1987) (noting that amendments to Texas’s protective order rule brought it closer to the language of Rule 26(c) and discussing federal protective order burdens); see also Benham, supra note 2, at 2191–93 (describing the federal protective-order framework).  
59 See, e.g., United States v. Int’l Bus. Machs. Corp., 67 F.R.D. 40, 47–48 (S.D.N.Y. 1975) (finding that no protection was warranted where no evidence supported a representation that information was confidential); cf. also 8A Charles Alan Wright et al., Federal Practice and Procedure § 2043 (3d ed. 2010) (noting that Rule 26(c) generally provides protection for confidential information, in addition to other categories of information).  
60 In re Ford Motor Co., 211 S.W.3d 295, 299–300 (Tex. 2006) (“Although a trial court often considers protective orders in the context of trade secrets, e.g., Garcia v. Peeples, 734 S.W.2d 343, 346 (Tex.1987), the express terms of the parties’ agreed protective order make clear that trade secrets are not the only materials worthy of protection.”).  
61 See Phillips ex rel. Estates of Byrd v. Gen. Motors Corp., 307 F.3d 1206, 1211 (9th Cir. 2002). Some courts have suggested that Rule 26(c) provides protection in some circumstances even when the information at issue is not “confidential research information.” Id. (“The law, however, gives district courts broad latitude to grant protective orders to prevent disclosure of materials for many types of information, including, but not limited to, trade secrets or other confidential research, development, or commercial information.”); cf. also Wright et al., supra note 59, § 2043 (dispelling argument that Rule 26(c) provides for protective orders only when
category of non-trade secret confidential information would be personal medical records: no one would dispute a litigant's legitimate interest in keeping medical information private, yet it could virtually never qualify as a trade secret. Still, the rule allows courts to limit the audience for medical records just as it does for trade secrets or other proprietary commercial information.

Second, to obtain an audience-limiting protective order, litigants must demonstrate that public dissemination of the confidential information would be seriously harmful. In cases involving trade secrets and commercial information, the harm put forward is typically economic. As discussed above, the theory goes that forcing litigants to disclose proprietary information, unprotected from competitors, devalues the information.

The supreme court has been unequivocal on the quantum of proof required to establish both prongs. Parties seeking protective orders must provide "a particular and specific demonstration of fact as distinguished from stereotyped conclusory statements." Moreover, "sweeping..."
predictions" or harm without "specific examples" are insufficient to support a protective order. This burden largely mirrors federal protective-order requirements.

B. Discovery Sharing

A discovery-sharing dispute gave the Supreme Court of Texas an opportunity to examine the contours of the protective-order burden. In Garcia v. Peeples, the court reviewed a trial judge’s broad protective order, putatively issued to protect General Motor’s trade secrets. The order forbade dissemination of vehicle design documents to anyone outside of the specific case. The critical question before the court: was the trial court’s order too broad where it stopped the plaintiff’s attorney from sharing the documents with other (non-competitor) attorneys involved in similar litigation?

Predictably, the sharing/trade secret issue arose in a product-liability case. Manuel Garcia, the plaintiff, was the sole survivor of a post-collision fuel-fed fire in a GM vehicle. He sued and requested fuel-system design documents from GM. GM produced the fuel-system documents in the case but asked the trial court to protect them from wider dissemination because the documents apparently contained trade secrets. The trial judge

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67 Garcia, 734 S.W.2d at 345.
68 See, e.g., Parsons v. Gen. Motors Corp., 85 F.R.D. 724, 726 (N.D. Ga. 1980) (denying protective order where allegations of confidentiality were not “particularized” and allegations of “competitive harm [were] vague and conclusory when specific examples are necessary”); see also MOORE, supra note 64, at § 26.102; WRIGHT ET AL., supra note 59, at § 2035 (“The courts have insisted on a particular and specific demonstration of fact, as distinguished from stereotyped and conclusory statements, in order to establish good cause.”); cf. Richard L. Marcus, A Modest Proposal: Recognizing (At Last) That the Federal Rules Do Not Declare That Discovery is Presumptively Public, 81 CHI.-KENT L. REV. 331, 348 (2006) (observing that the protective order burden is “somewhat exacting” but not an insurmountable hurdle that would create public access right).
69 See Garcia, 734 S.W.2d at 344–45.
70 Id.
71 Id. at 346.
72 Id. The court also decided two collateral issues in Garcia, holding that certain notes and indexes were attorney work product and also allowing GM to enforce protective orders from other jurisdictions. See id. at 348–49.
73 Id. at 344.
74 Id.
75 See id. at 344–45.
(David Peeples) issued an onerous protective order that, among other restrictions, allowed only the plaintiff, his attorneys, and his experts to access the documents. 76

Garcia sought mandamus relief, contending that GM's evidence did not support the order's breadth. 77 In particular, Garcia contended that he should be allowed to share the fuel-system-design information with litigants involved in similar litigation against GM. 78 Doing so, the reasoning went, would not harm GM because litigants in product-liability cases were almost certainly not competitors. 79 Moreover, Garcia contended that public policy favored discovery sharing as a mechanism to encourage full candor in discovery and a method to increase court efficiency. 80

The supreme court agreed. 81 Justice Kilgarlin, writing for the majority, observed that GM did have a legitimate interest in keeping its trade secrets from competitors. 82 But the court went on to hold that sharing discovery information between non-competitor litigants would not harm GM in a manner that outweighed the public policies favoring sharing. 83

The court accepted at least two of the oft-stated policy rationales that support sharing: discovery integrity and litigation efficiency. With respect to the first, the court bemoaned "the lack of candor during discovery in complicated litigation." 84 Parties in cases with similar discovery requests and shared discovery, the court reasoned, "are forced to be consistent in their responses by the knowledge that their opponents can compare those responses." 85

76 See id. at 346 n.2.
77 Id. at 345–46.
78 Id. at 346.
79 See id. at 348.
80 Id. at 346–47.
81 Id. at 348.
82 Id.
83 Id.
84 Id. at 347. Discovery sharing's propensity to increase candor in disclosure is a laudable feature even without sharing's efficiency benefits. See, e.g., id. Likewise, sharing creates the ability for plaintiff's counsel to collaborate in discovery for similar cases—a practice that would be forbidden in many instances in a non-sharing regime. A byproduct of this collaboration may very well be increased efficiency as a result of better-tailored discovery requests. Cf., e.g., Patterson v. Ford Motor Co., 85 F.R.D. 152, 153–54 (W.D. Tex. 1980); cf. also Benham, supra note 2, at 2199, 2206.
85 Garcia, 734 S.W.2d at 347.
The court also recognized the obvious efficiencies of discovery sharing. A non-sharing system "forces similarly situated parties to go through the same discovery process time and time again, even though the issues involved are virtually identical." A sharing order, on the other hand, would allow parties in similar cases to benefit from previous discovery while denying the defendant in those cases the undue benefit of requiring re-discovery by each party bringing a suit against it.

The Garcia court found that the protective order was too broad. Importantly, GM’s legitimate interest in the protective order was to prevent dissemination to competitors, not non-competitor litigants like Garcia. Garcia left Texas courts with several important takeaways for issuing protective orders in trade secret cases. First, parties that produce trade secret information in discovery are typically entitled to an order protecting the information from competitors. Second, a party seeking such protection must produce specific, concrete evidence that it will indeed be harmed in the absence of the order. Third, the court implicitly held that protective orders must be no broader than the evidence supports. If evidence only supports a party’s contention that it will be harmed by disclosure to Person A, a protective order preventing dissemination to both Person A and Person B is overbroad (assuming that under the more lenient order Person B would be forbidden from providing Person A with the information). Fourth, courts should consider the systemic impact of orders restricting the dissemination of discovery information. These systemic considerations—discovery

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86 Id.
87 See id. at 348; cf. also In re Quality Safety Sys. Co., No. 05-10-00801-CV, 2010 WL 4192897, at *1 (Tex. App.—Dallas Oct. 26, 2010, no pet.) (mem. op.) (citing Garcia to deny petition for writ of mandamus seeking to limit discovery sharing with third parties); Am. Honda Motor Co. v. Dibrell, 736 S.W.2d 257, 259 (Tex. App.—Austin 1987, no writ) (holding that trial court did not abuse its discretion by entering sharing order in case involving trade secrets). But see In re Universal Coin & Bullion, Ltd., 218 S.W.3d 828, 833 (Tex. App.—Beaumont 2007, pet. denied) (warning, in dicta, that potential protective order was not adequate where it did not limit sharing to suits concerning the same subject matter).
88 See Garcia, 734 S.W.2d at 348.
89 Id.
90 Id.; cf. also In re Alford Chevrolet-Geo, 997 S.W.2d 173, 189 (Tex. 1999) (stating that in Garcia, the court "held that a motion for protection from discovery must be based on 'a particular, articulated and demonstrable injury'").
91 Garcia, 734 S.W.2d at 348.
92 Id. at 346–47.
discovery and litigation efficiency—obviously extend beyond the proprietary interests of the parties to the litigation. A few years after Garcia, then-Justice (now-Senator) Cornyn, writing for the majority, reaffirmed the court’s commitment to discovery sharing. In Eli Lilly & Co. v. Marshall, the court considered the propriety of an order compelling production of information that a pharmaceutical company previously submitted to the FDA. The information related to the health care provider’s reports about problems with the drug Prozac, and no party contended that the information comprised trade secrets. Instead, the pharmaceutical company resisted production on the basis that the FDA regulations made the information secret.

While the court did find that the trial court abused its discretion by ordering production of at least some of the information, it went on to express its commitment to shared discovery. Justice Cornyn observed that “under the doctrine of shared discovery, the fruits of discovery are available not only to the parties in a particular case but may be disseminated in turn to other litigants and potential litigants.” Indeed, the court noted that with respect to the discoverable portion of the FDA information, the requesting parties were entitled to “to share that discovery with their expert witnesses and litigants in other cases.”

C. Implicit Sharing Ban?

While the supreme court has revisited the discoverability of trade secrets several times, it has not directly addressed trade-secret discovery-sharing

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93 With all protective-order determinations, the evidence supporting the order matters. One might read Garcia to mean that protective orders must always include sharing provisions, but this interpretation ignores the case-by-case nature of the inquiry. One feature of Garcia is undoubtedly mandatory—trial courts should not enter protective orders absent evidence of significant and serious harm that would occur absent the order. Id. at 248. Because well-crafted sharing provisions almost always exclude competitors from access to discovery materials and prevent discovery-dissemination-based harms, it follows that sharing orders are mandatory in most cases.

94 850 S.W.2d 155, 156–57 (Tex. 1993).
95 Id. at 156–57, 160.
96 Id. at 157.
97 Id. at 160.
98 Id.
99 Id.
since Garcia. Nonetheless, according to opponents of sharing, the court implicitly overruled Garcia in a later trade secret case, In re Continental. This argument is flawed for several reasons, as discussed in Part III. Still, it is worth examining In re Continental—the case sheds light on the relationship between the discoverability of trade secrets and the best methods to protect them during litigation.

In re Continental said much about when trial courts may order production of trade secrets. But it said little to nothing about whether parties may share the information after exchanging it. In In re Continental, a trial court ordered a defendant tire company to produce its “skim stock” formula—essentially a portion of the tire’s ingredients. The plaintiffs conceded that the formula was a trade secret. Thus, the issue in the case was whether the qualified trade secret privilege (Texas Rule of Evidence 507) allowed the tire company to withhold the information in discovery.

Texas Rule of Evidence 507 provides a privilege to withhold trade secret information when doing so does not “tend to conceal fraud or otherwise work injustice,” subject to an “appropriate protective order.” In In re Continental, the court grappled with exactly when courts are allowed to order production of trade secret information in discovery to prevent “injustice.”

There are at least three ways to approach the trade secret discoverability problem in the routine (non-fraud) case. First, courts could allow discovery of the information so long as it is relevant to the case. The In re Continental court rejected this approach, reasoning that if a bare relevance threshold could defeat the trade secret privilege, Rule 507 would be

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100 See, e.g., In re Bass, 113 S.W.3d 735, 737 (Tex. 2003); In re Cont’1 Gen. Tire, Inc., 979 S.W.2d 609, 610 (Tex. 1998).
101 See, e.g., Zappe v. Medtronic USA, Inc., No. C-08-369, 2009 WL 792343, at *1 (S.D. Tex. Mar. 23, 2009) (reading In re Continental to approve a non-sharing order); In re Cont’l, 979 S.W.2d at 615.
102 See In re Cont’l, 979 S.W.2d at 612–14.
103 Id. at 610.
104 Id. at 615.
105 Id. at 610.
106 TEX. R. EVID. 507.
107 In re Cont’l, 979 S.W.2d at 613.
108 Id. at 610–13.
109 Id. at 613–14.
rendered meaningless. Indeed, information that is not relevant is generally not discoverable in any event, making relevance an illusory floor in trade secret cases. A second approach (advocated by the defendants in *In re Continental*) reads Rule 507 as something approaching an absolute privilege. According to this line of reasoning, a protective order “can never adequately protect a sensitive trade secret” because of the risk of intentional or inadvertent disclosure. The court rejected this approach because it would effectively nullify the qualification language in Rule 507 that expressly allows production of trade secrets in certain circumstances. But the court noted that trial judges should balance “potential inadequacies” of protective orders when deciding to compel production of trade secrets (or not).

The court settled on a third approach, somewhere in the middle, requiring parties requesting trade secrets to demonstrate “necessity.” When a party establishes that information sought in discovery comprises trade secrets, “[t]he burden . . . shifts to the requesting party to establish that the information is necessary for a fair adjudication of its claims.” The court went on to hold that the plaintiffs in *In re Continental* had not established that the tire formula was necessary for a fair adjudication of its claims and barred discovery of the information.

Along the way to this holding, the court dropped a footnote that has engendered a wave of anti-sharing litigation, multiple mandamus proceedings across the state, and several granted petitions for review by the supreme court. When noting that trial courts that order trade secret

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110 Id.
111 *See* TEX. R. CIV. P. 192.3 (“In general, a party may obtain discovery regarding any matter that is not privileged and is relevant to the subject matter of the pending action”).
112 *In re Cont'l*, 979 S.W.2d at 614.
113 Id.
114 *See id.*
115 Id.
116 *See id.* at 613.
117 Id.
118 *See id.* at 615.
production must do so subject to an appropriate protective order, the court (in its rift-creating footnote) wrote, “In this case, for example, the trial court limited access to the information to the parties in this lawsuit, their lawyers, consultants, investigators, experts and other necessary persons employed by counsel to assist in the preparation and trial of this case.”\footnote{120} In other words, a non-sharing order was apparently appropriate in the \textit{In re Continental} proceeding.

This murky footnote, undoubtedly dicta, led to arguments that the supreme court had implicitly overruled Garcia’s holding that sharing provisions were often required in protective orders.\footnote{121} And the arguments went further—after \textit{In re Continental}, many litigants argued that the supreme court had actually forbidden discovery sharing altogether.

### III. THE ATTACK ON DISCOVERY SHARING

Litigants (usually large corporate interests) have asked the supreme court to forbid discovery sharing in Texas trade secret cases multiple times in the past decade.\footnote{122} And since 2004, the court has agreed to hear the issue at least three times, though it has never issued an opinion revisiting the Garcia question.\footnote{123} If granted, the requests to overrule Garcia and prohibit sharing would undercut the practice in sharing jurisdictions across the country.

To make these extraordinary requests to change the law seem plausible, the proponents usually conflate the standard governing the discoverability of trade secrets with the standard for protecting them after disclosure.\footnote{124} Sharing protective orders in trade secret cases, the reasoning goes, would nullify Texas Rule of Evidence 507 (a rule aimed at discoverability, not protective-order standards).\footnote{125}

The typical three-part attack on Garcia and sharing in trade secret cases:

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120 \textit{In re Cont'l}, 979 S.W.2d at 613 n.3.
122 See Ambrose, supra note 6.
123 \textit{Id}.
124 See, e.g., Automobile Manufacturers’ Amicus Brief, supra note 3.
125 See, e.g., id. (“Sharing orders eliminate [Rule 507’s] requirement that necessity be demonstrated on a case-by-case basis.”).
\end{verbatim}
To obtain trade secret information in discovery, Rule 507 requires requesting parties to establish that the information is necessary to prove a claim or defense.

Similarly situated third-party litigants who would receive the information under a sharing protective order must individually demonstrate that the information is necessary in their particular cases.

If courts enter sharing protective orders that allow parties to disseminate trade secret information to similar third-party litigants, those courts ignore Rule 507’s necessity requirement.

Only the first of these three propositions is demonstrably true.126 In re Continental itself belies the other two.127 Indeed, In re Continental separates the trade secret discoverability inquiry (one that allows discovery of trade secrets (absent fraud) only if they are necessary proof in the case) from the standard governing the adequacy of audience-limiting protective orders.128

The case actually held that after trial courts determine that trade secret information “is necessary for a fair adjudication” of the requesting party’s claims, trial courts should “ordinarily” compel production of the information subject to “an appropriate protective order.”129 The term “protective order,” as used in In re Continental, plainly refers to an order that was available under former Texas Rule of Civil Procedure 166b(5)—titled “Protective Orders”—and succeeded by identically titled Rule 192.6.130 The court correctly recognized, consistent with decades of similar decisions in Texas and around the country, that a protective order is the appropriate mechanism to limit the audience for otherwise discoverable information.131

127 See id. at 611–13.
128 See id. at 613.
129 See id. (emphasis added).
131 See In re Cont’l, 979 S.W.2d at 613; see also, e.g., Glennede Tr. Co. v. Thompson, 56 F.3d 476, 483 (3d Cir. 1995) (recognizing protective orders as method to limit discovery access); Garcia v. Peeplees, 734 S.W.2d 343, 345 (Tex. 1987) (evaluating propriety of protective order to limit access to trade secrets in discovery); cf. In re Terra Int’l, Inc., 134 F.3d 302, 306 (5th Cir. 1998) (allowing parties to limit the audience when discovery is conducted).
In re Continental thus acknowledged two important pieces of pretrial-discovery and protective-order bedrock: (1) the audience-limiting protective-order inquiry is distinct from the discoverability inquiry, and (2) some protective orders are “appropriate” to protect trade secret discovery information while others are not.

By using the modifier “appropriate” before “protective order,” the court did indeed recognize that some protective orders might fail because they do not satisfactorily protect trade secrets. Likewise, some protective orders might not be “appropriate” because they are too severe, restricting disclosure to an audience more narrow than evidence of harm would support.

Thus, the question in trade secret-sharing cases is whether narrowly drawn sharing protective orders adequately protect otherwise discoverable trade secret information and are therefore “appropriate.” The question is not (as those attacking discovery sharing would contend) whether other similarly situated litigants must establish “necessity” under Rule 507 after the discovering party has already done so.

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132 See In re Cont’l, 979 S.W.2d at 613; Chapa v. Garcia, 848 S.W.2d 667, 678 n.8 (Tex. 1992) (Doggett, J., concurring) (“While discoverability by the parties is often confused with disclosability to the public, discoverability and disclosability issues must be resolved separately.”). No doubt the two inquiries inform one another—courts should consider the efficacy of protective measures when deciding to order production of trade secrets or other sensitive information. See In re Cont’l, 979 S.W.2d at 614.

133 See id.

134 See id.

135 Cf., e.g., ActiveVideo Networks, Inc. v. Verizon Commc’ns, Inc., 274 F.R.D. 576, 584 (E.D. Va. 2010) (refusing to enter protective-order provision that would have denied in-house counsel access to trade secrets and other confidential information in lawsuit between competitors).

136 Even if courts were required to consider “necessity” before allowing sharing orders in trade secret cases, most already do so (at least implicitly) when crafting the sharing provision in the order. See Raymond Handling Concepts Corp. v. Superior Court, 45 Cal. Rptr. 2d 885, 888 (Cal. Ct. App. 1995) (rejecting argument that necessity requirement of California trade secret privilege foreclosed sharing protective orders and noting that “[s]ince plaintiff’s attorney may share this discovery only with counsel in other similar cases, it must be assumed that the information is also discoverable in these other similar cases”). The sharing provision in a sharing protective order defines the class of similar litigants who are entitled to receive the discovery information. Sharing provisions are often quite specific. So, for instance, a sharing provision might provide that the sharing class includes all persons with pending claims against the defendant in the sharing case for injuries stemming from the particular product at issue in the sharing case. Assuming the discovery at issue is necessary to resolve the sharing case, it would presumably be relevant and necessary in the receiving cases as well. See id. Product design information, for
Two uncontroversial legal principles support framing the inquiry in this way. First, absent a valid protective order, litigants may freely distribute information that they obtain in discovery. Thus, discovery sharing, and even public dissemination, is the default without a valid order to the contrary.

Second, a contested protective order is valid only where the party seeking it establishes good cause (or an analogous legal standard) for the order by producing concrete evidence of a serious and clearly defined injury. Federal courts and state courts routinely reject requests for non-sharing orders because inadequate (or no) evidence of competitive harm supports the requests. By doing so, courts also further their own interest (and the public's interest) in litigation efficiency.

Proponents of a no-discovery-sharing regime reject this evidence-based approach and the efficiency benefits that flow from it. They would

instance, would likely be necessary in any case where the parties allege the product is defective. Assuming the sharing provision in the protective order limits sharing to cases where parties allege the product is defective, the court has effectively found the information necessary in those later cases.

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137 See, e.g., Seattle Times Co. v. Rhinehart, 467 U.S. 20, 37 (1984); Exum v. U.S. Olympic Comm., 209 F.R.D. 201, 205 (D. Colo. 2002) ("Parties to litigation have a First Amendment right to disseminate information they obtained in discovery absent a valid protective order."); see also infra Part III.B.

138 See, e.g., Masinga v. Whittington, 792 S.W.2d 940, 940 (Tex. 1990) (holding that party "must show particular, specific and demonstrable injury by facts sufficient to justify a protective order").

139 See, e.g., Kamp Implement Co. v. J.I. Case Co., 630 F. Supp. 218, 221 (D. Mont. 1986) (ruling that "burden will be upon defendants to make a specific showing of harm or competitive disadvantage which will result from disclosure" to similar litigants); cf. Benham, supra note 2, at 2191–93.

140 See, e.g., Garcia v. Peeples, 734 S.W.2d 343, 347 (Tex. 1987) ("[S]hared discovery makes the system itself more efficient."); Richard L. Marcus, The Discovery Confidentiality Controversy, 1991 U. ILL. L. REV. 457, 464–66, 466 n.61, 495–96 (1991) (endorsing at least some form of discovery sharing, noting pro-sharing state legislation); Miller, supra note 8, at 498–99 (embracing sharing where it furthers efficiency); see also HARE, JR. ET AL., supra note 7, at 69–70 (observing that non-sharing protective orders mean that discovery "must be repeated anew in every case").

instead inject a de facto presumption of harm into every trade secret case to justify forbidding sharing protective orders categorically.\textsuperscript{142}

But a no-evidence-required take on protective orders would nullify decades of Texas law and would put the Supreme Court of Texas in conflict with federal and state courts across the country.\textsuperscript{143} A discovery-sharing ban in trade secret cases would also make litigation more expensive and run contrary to Texas procedural reform aimed at increasing litigation efficiency.

\textbf{A. Evidence-Based Protective-Order Standards}

As detailed in Section II.A, Texas and federal courts require parties requesting protective orders to produce evidence of "a particular, articulated and demonstrable injury, as opposed to conclusory allegations."\textsuperscript{144} Along the same lines, courts have long recognized that in the context of trade secrets or confidential commercial information, parties must establish that an economic or competitive harm would occur without entry of a protective order.\textsuperscript{145}

Despite this baseline proof requirement, courts have undeniably broad discretion in tailoring protective orders, "frequently finding protection justified and frequently denying protection."\textsuperscript{146} This discretion is rooted in

\begin{footnotesize}
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\item\textsuperscript{142} Id. Florida courts, for instance, have found sharing protective orders to be inconsistent with that state's trade secret privilege. Id. In \textit{Wal-Mart v. Endicott}, an intermediate appellate court held that a sharing protective order conflicted with Florida's qualified trade secret privilege. Id. Moreover, the court found that the sharing order's failure to adequately identify litigants with similar pending claims would harm Wal-Mart's interests, whether competitors were in the sharing class or not. See id.

\item\textsuperscript{143} See, e.g., Raymond Handling Concepts Corp. v. Superior Court, 45 Cal. Rptr. 2d 885, 888 (Cal. Ct. App. 1995) (holding trial court did not abuse its discretion by allowing sharing order in case involving trade secrets). \textit{But see Endicott}, 81 So. 3d at 490.

\item\textsuperscript{144} Masinga v. Whittington, 792 S.W.2d 940, 940 (Tex. 1990); \textit{Garcia}, 734 S.W.2d at 345.

\item\textsuperscript{145} See, e.g., Glenmede Tr. Co. v. Thompson, 56 F.3d 476, 484 (3d Cir. 1995) (finding that parties seeking protective order failed to establish harm from disclosure and refusing to upset trial court's denial of protective order); \textit{see also}, e.g., Parsons v. Gen. Motors Corp., 85 F.R.D. 724, 726 (N.D. Ga. 1980) (denying protection where GM failed to prove that discovery information was "confidential and that disclosure [would have create[d] a competitive disadvantage for the party]").

\item\textsuperscript{146} WRIGHT ET AL., \textit{ supra} note 59, at § 2036; \textit{see also} Benham, \textit{ supra} note 2, at 2192.
\end{enumerate}
\end{footnotesize}
trial courts' unique position in managing the pretrial discovery process and the fact-intensive nature of the protective-order inquiry. But discretion does have limits. As guidance, several federal circuits have articulated factors to shepherd trial courts exercising protective-order discretion. For instance, in a widely cited analysis from *Glenmede Trust Co. v. Thompson*, the Third Circuit held—consistent with the Texas high court's public policy-based approach in *Garcia*—that courts should consider, among other factors, "whether the sharing of information among litigants will promote fairness and efficiency."

Thus, along with Texas courts, federal courts have constructed a protective-order system of bounded discretion, demarcated by proof of good cause and influenced by public policy considerations. And like Texas courts, federal courts value discovery sharing, though courts in the federal system differ with one another on how best to accomplish it. Some federal courts enter sharing protective orders. Others disfavor upfront sharing protective orders and instead prefer later, case-by-case modification to allow sharing.

**B. The Freedom to Disseminate Discovery Information**

If a court does not find adequate cause for a protective order, parties are free to disseminate the materials to other litigants or the public at large. Thus, the decision to "allow" discovery sharing is actually a decision not to enter a protective order to forbid it. Over the past four decades, the idea that

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147 See, e.g., Seattle Times Co. v. Rhinehart, 467 U.S. 20, 36 (1984) ("To be sure, Rule 26(c) confers broad discretion on the trial court to decide when a protective order is appropriate and what degree of protection is required.").

148 See, e.g., Benham, supra note 2, at 2192 (citing, e.g., *In re Roman Catholic Archbishop of Portland in Or.*, 661 F.3d 417, 424 (9th Cir. 2011) (applying multi-factor analysis to assess "good cause" for protective order)).

149 56 F.3d at 483; cf. *Garcia*, 734 S.W.2d at 348 (holding that sharing promotes "public policies" of efficient, transparent court operations).


151 See Bertetto v. Eon Labs, Inc., Civ. No. 06-1136 JCH/ACT, 2008 WL 2522571, at *2 (D.N.M. May 29, 2008) (rejecting a sharing provision in preference to a system of case-by-case protective-order modification). Some might argue that sharing decisions should be made on a case-by-case basis through after-the-fact protective order modifications. Modifying protective orders on a case-by-case basis, however, is often less efficient than Texas's current sharing-protective-order framework. See Benham, supra note 10, at 1781.

discovery can be made public unless a court orders otherwise has become entrenched.\textsuperscript{153} This freedom, it turns out, has a constitutional root.

In \textit{Seattle Times Co. v. Rhinehart}, the United States Supreme Court considered whether a litigant had a First Amendment right to publish pretrial discovery information.\textsuperscript{154} The dispute began when a Washington state trial court entered a protective order in a quirky defamation case.\textsuperscript{155} The order forbade a defendant newspaper from publishing religious information it obtained in discovery from the defamation plaintiffs (a religious sect and its leader).\textsuperscript{156}

Writing for the Court and striking a pragmatic tone, Justice Lewis Powell observed that civil discovery can be particularly invasive.\textsuperscript{157} Nonetheless, the Court held that the First Amendment protects the dissemination of pretrial discovery.\textsuperscript{158} Ultimately, however, the Court also held that discovery was a special context, and thus protective orders were not the type of prior restraints that would require the usual exacting First Amendment scrutiny.\textsuperscript{159}

Instead, the Supreme Court held that protective orders satisfy the First Amendment only where they are \textit{"entered on a showing of good cause as required by Rule 26(c), [are] limited to the context of pretrial civil discovery, and [do] not restrict the dissemination of the information if}\n
\begin{footnotesize}
\begin{enumerate}
\item Seattle Times Co. v. Rhinehart, 467 U.S. 20, 22 (1984); see also Benham, \textit{supra} note 10, at 1781.
\item See \textit{Seattle Times Co.}, 467 U.S. at 26–27.
\item See \textit{id.} at 27.
\item See \textit{id.} at 34–35.
\item See \textit{id.} at 31 ("It is, of course, clear that information obtained through civil discovery authorized by modern rules of civil procedure would rarely, if ever, fall within the classes of unprotected speech identified by decisions of this Court.").
\item See \textit{id.} at 33–34. \textit{Seattle Times} is often cited for the blanket proposition that there is no First Amendment right of "access" to pretrial discovery materials. \textit{See, e.g., Bond v. Utreras}, 585 F.3d 1061, 1077 (7th Cir. 2009). \textit{Seattle Times} does so hold, but this aspect of the case does not speak to whether parties may \textit{disseminate} discovery. Parties may not have a protected right to access discovery information, but they do have a First Amendment right to \textit{disseminate} discovery information. \textit{Seattle Times Co.}, 467 U.S. at 37. This speech interest may be restricted only by a protective order that satisfies \textit{Seattle Times}' requirements. \textit{Id.}
\end{enumerate}
\end{footnotesize}
gained from other sources . . . "160 Thus, courts that enter protective orders without good cause (or presumably a standard requiring a similar evidentiary showing) violate the First Amendment in addition to ignoring the requirements of the applicable rules of civil procedure.

The evidence-based good cause analysis approved in Seattle Times works to constrict the breadth of protective orders. The decision to grant or deny a protective order is not binary: A court considering a protective-order request does not simply decide to enter an order or not. Instead, courts must evaluate whether the scope and breadth of the particular order is justified.161

At one end of the spectrum, an audience-limiting protective order might limit the audience for discovery materials to an in camera review.162 At the other end, a court might deny a protective-order request altogether, allowing widespread public dissemination of discovery materials.163

The distinction between the two scenarios, and scenarios along the spectrum in between, often lies in differences between the proof of harm put forward by the party seeking the order. Protective orders crafted on a proof-of-harm basis answer the concern that litigants engaged in intrusive discovery might suffer serious harm without a sufficient audience limitation (e.g. an order forbidding access to competitors or the media). But the proof-of-harm requirement also protects speakers who have a right to share what they learn in discovery when doing so is not harmful.

Presuming harm (expressly or implicitly) in trade secret cases through an outright ban on discovery sharing would turn this evidence-based

160 See Seattle Times Co., 467 U.S. at 37 (emphasis added). Courts are divided on whether the proper First Amendment test for protective orders is simple good cause or intermediate scrutiny. Cf. In re Requests for Investigation of Attorney E., 78 P.3d 300, 310 (Colo. 2003) (en banc) (applying intermediate scrutiny to a protective order under an attorney discipline rule analogous to Rule 26(c)). For a full discussion of the split and its implications, see Benham, supra note 10, at 1784–85. For purposes of this case, and without conceding that the good cause standard sufficiently protects plaintiffs' speech rights, it is incontestable that good cause is the minimum standard a protective order must meet to satisfy the First Amendment. See Seattle Times Co., 467 U.S. at 37.

161 See Seattle Times Co., 467 U.S. at 36 (Protective-order rule “confers broad discretion on the trial court to decide when a protective order is appropriate and what degree of protection is required.” (emphasis added)).


approach on its head, obviating the First Amendment burden typically placed on parties seeking speech-restricting protective orders.164

C. Competitor Cases

One argument against sharing protective orders is that attorneys in the sharing class (representing similar litigants, not competitors of the producing party) might inadvertently or intentionally leak protected documents.165 Those documents, the reasoning goes, could then fall into the hands of competitors.

But how do courts address the risk of harmful disclosure in the higher risk context of cases between competitors? It turns out that they require specific and substantial evidence of harm before denying access to proprietary discovery information, even in cases involving direct competitors.166

For example, in Volvo Penta of the Ams., Inc. v. Brunswick Corp., a federal district court refused to enter an onerous “outside-counsel-only” protective-order provision in a competitor case.167 This provision would have prevented virtually everyone but the parties’ outside counsel from viewing discovery information.168 The court declined to include the provision because there was no evidence that an in-house lawyer was involved in competitive decision making for her employer.169

In Volvo, like most complex cases, both parties had agreed that some form of protective order was appropriate.170 The disagreement before the court was which of two competing orders was adequate—a narrower version allowed in-house counsel access while a broader version forbade it.171 The court’s decision was particularly high stakes because Volvo and Brunswick were apparently “hostile” competitors.172

164 See, e.g., Kamp Implement, 630 F. Supp. at 220 (approving sharing protective order and recognizing that the “burden” to obtain a non-sharing order remains “squarely upon defendants, as is required by Rule 26(c) and the first amendment”) (internal quotations omitted).
166 See id. at 242.
167 Id. at 245.
168 See id. at 241.
169 Id. at 242–45.
170 Id. at 241.
171 See id.
172 See id.
The district court, citing the seminal circuit case on outside-counsel protective orders, denied the outside-counsel-only provision.\textsuperscript{173} The court went on to observe that Brunswick’s in-house counsel testified in an affidavit that she had no role in “competitive decision making.”\textsuperscript{174} Volvo produced no specific contrary evidence to establish that disclosing the documents to the in-house lawyer would harm its competitive position other than to contend she \textit{might} inadvertently disclose the information to someone in her company with the power to make a competitive decision.\textsuperscript{175}

The court recognized the risk of inadvertent disclosure by an otherwise protective-order-abiding in-house attorney but noted that in-house lawyers “like any other retained attorney, must serve as ‘officers of the court’ and must abide by the ‘same Code of Professional Responsibility and ethics.’”\textsuperscript{176} As a result, the court “could not merely assume that in-house attorneys would allow confidential information to fall into the hands of their employer.”\textsuperscript{177} After concluding that no evidence indicated that Brunswick’s in-house lawyer played a role in the company’s competitive decision making, the court held that it should enter the less restrictive protective order and allow her access.\textsuperscript{178}

\textit{Volvo} is one among dozens of representative cases applying the “competitive-decision-making” analysis to limit the scope of protective orders in direct competitor cases.\textsuperscript{179} In many of these cases, including decisions emanating from Texas federal courts, trial judges allow one competitor’s in-house counsel access to another competitor’s proprietary information.\textsuperscript{180} And in many instances, courts do so because the party seeking to exclude in-house lawyers from viewing the information does not put forward specific evidence of serious harm that would flow from such a

\textsuperscript{173} See \textit{id.} at 243.

\textsuperscript{174} \textit{Id.} at 244.

\textsuperscript{175} See \textit{id.} at 243.

\textsuperscript{176} \textit{Id.} (quoting U.S. Steel Corp. v. United States, 730 F.2d 1465, 1468 (Fed. Cir. 1984)).

\textsuperscript{177} \textit{Id.}

\textsuperscript{178} See \textit{id.} at 243–45.

\textsuperscript{179} See also, e.g., ActiveVideo Networks, Inc. v. Verizon Commc’ns, Inc., 274 F.R.D. 576, 583–84 (E.D. Va. 2010).

disclosure—even where the lawyer works directly for the competing company.\textsuperscript{181}

Like in-house attorneys who are allowed access to their competitors’ trade secrets, the non-competitor attorneys in the typical discovery-sharing case who would receive trade secret information under the sharing provision should be required to agree not to disclose the information inappropriately.\textsuperscript{182} And although there is some negligible risk of inadvertent disclosure under any protective order, sharing or non-sharing, attorneys receiving shared discovery “must serve as ‘officers of the court’ and must abide by the ‘same Code of Professional Responsibility’ and ethics” as the attorneys who first receive the information in the original case.\textsuperscript{183}

A similar argument against sharing posits that protective orders have been violated in the past and therefore could be violated in the future.\textsuperscript{184} But this argument ignores the reality that all protective orders, sharing and non-sharing, can be violated. Thus, if one accepts a version of the world where the violability of protective orders means they are always inadequate, no protective order would ever suffice to protect trade secret information. Some have suggested as much—arguing to the court that all protective orders may be insufficient to protect trade secrets.\textsuperscript{185} Accepting this argument could mean Texas Rule of Evidence 507 would function much like an absolute privilege—trade secrets would be beyond litigants’ reach, even if justice depended on their disclosure.

By its own language, Rule 507 is not an absolute privilege, however.\textsuperscript{186} The court recognized this, holding that “protective orders” may be “appropriate” to protect trade secrets and rejecting a contention that Texas Rule of Evidence 507 should function like an absolute privilege.\textsuperscript{187} To accept the position that speculative, unspecified protective-order violations

\footnote{\textit{See}, \textit{e.g.}, \textit{id.}}

\footnote{\textit{See}, \textit{e.g.}, Garcia v. Peeples, 734 S.W.2d 343, 348 (Tex. 1987) (noting that trial courts can require parties to agree not to disclose shared discovery information inappropriately).}

\footnote{\textit{See Volvo Penta of the Ams., Inc.}, 187 F.R.D. at 243 (quoting U.S. Steel Corp. v. United States, 730 F.2d 1465, 1468 (Fed. Cir. 1984)).}

\footnote{\textit{Cf.}, \textit{e.g.}, Brief of Amicus Curiae Product Liability Advisory Council, Inc., In Support of Relator at 7, 9–12, \textit{In re Cont’l Tire of the Ams., LLC} (No. 12-0124), 2012 WL 6042916 (Tex. May 7, 2012).}

\footnote{\textit{Id.} at 7 (“...the reality is that protective orders in trade secret cases frequently do not work . . . .”).}

\footnote{\textit{See} TEX. R. EVID. 507.}

\footnote{\textit{See \textit{In re Cont’l Gen. Tire, Inc.}, 979 S.W.2d 609, 612–13 (Tex. 1998).}
make protective orders unsuitable is to accept that the second half of Rule 507, which provides for the disclosure of trade secrets pursuant to protective orders, is meaningless. This absolute reading of Rule 507 is inconsistent with Texas and federal law.

D. Modification and Jurisdiction Issues

Perhaps one explanation for Texas’s affinity for sharing protective orders is a possible limitation on Texas courts’ jurisdiction to modify protective orders after a final judgment.

Federal courts, by contrast, have long recognized that parties or non-parties (including similar litigants, media, and members of the public) may intervene and request to modify a protective order. This is even true long after cases settle or otherwise reach final judgment.

Many federal courts, in fact, prefer later protective-order modifications to upfront, Garcia-style sharing provisions. To understand the difference between an upfront sharing provision and a later modification, imagine that in Case 1, Party X sues Corporation Y alleging that Y’s widget injured X. The court in Case 1 enters a non-sharing protective order, allowing X and Y to use discovery information only for the purpose of resolving Case 1. Case 1 settles and is disposed of through a final order or judgment.

Some years later, Party A sues Corporation Y in Case 2, alleging that Y’s widget injured A. Party A would like to use discovery from Case 1 (same defendant, same widget) to avoid having to repeat the efforts of Party X.

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188 See TEX. R. EVID. 507.
189 See In re Cont’l, 979 S.W.2d at 614 (rejecting tire manufacturer’s argument that the Rule 507 trade secret protection should operate as an “absolute” privilege).
190 See Times Herald Printing Co. v. Jones, 730 S.W.2d 648, 649 (Tex. 1987) (per curiam) (holding that trial court did not have power to “unseal” litigation documents after plenary power expired).
191 See, e.g., United Nuclear Corp. v. Cranford Ins. Co., 905 F.2d 1424, 1427 (10th Cir. 1990); cf. Benham, supra note 2, at 2210.
192 See Pub. Citizen v. Liggett Grp., Inc., 858 F.2d 775, 782 (1st Cir. 1988) (“We note that the courts and commentators seem unanimous in finding such an inherent power to modify discovery-related protective orders, even after judgment, when circumstances justify.”); see also MOORE, supra note 64, at ¶ 26.106[1] (“As long as a protective order remains in effect, the court that entered the order retains the power to modify it, even if the underlying suit has been dismissed.
193 See Benham, supra note 2, at 2228–29.
Because the protective order in Case 1, however, is non-sharing, Party X cannot share the information with Party A. Party A may, however, petition the court in Case 1 to modify its protective order to allow Party A to use the Case 1 information in Case 2. Under federal law, the court in Case 1 has ongoing jurisdiction to do so, and courts routinely engage in such modifications.  

Texas case law, on the other hand, gives a less-than-clear answer on post-plenary protective-order jurisdiction. In April 1987, a few months before the Texas Supreme Court decided *Garcia v. Peeples*, it decided a lesser-known case that arguably undermined trial-court power to modify existing protective orders.  

In *Times Herald Printing Co. v. Jones*, a non-party newspaper moved to unseal court files and discovery materials in a civil lawsuit more than five months after an agreed final judgment in the case.  

Chief Justice Hecht, then presiding trial judge of the 95th District Court in Dallas, denied the motion. The Dallas Court of Appeals affirmed, agreeing that the trial court had jurisdiction to consider the motion and affirming on the merits.  

On writ of error, the Texas Supreme Court reversed in a summary opinion, holding that the trial court’s plenary power over the sealing order had expired pursuant to Texas Rule of Civil Procedure 329b. At a minimum, *Times Herald* raises questions about a trial court’s power to modify protective orders after cases settle or otherwise reach a final judgment. And one could speculate that *Garcia v. Peeples*, decided months later in July 1987, could very well have been the court’s pragmatic recognition that *Times Herald* made sharing through later, post-plenary protective-order modifications untenable.

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194 See, e.g., *United Nuclear*, 905 F.2d at 1427 (relying on continuing jurisdiction to modify protective orders); see also Benham, *supra* note 2, at 2228–29.

195 *Times Herald*, 730 S.W.2d at 648.

196 717 S.W.2d 933, 935 (Tex. App.—Dallas 1986), vacated and dismissed, 730 S.W.2d 648 (Tex. 1987).

197 *Id.* at 933.

198 *Id.* at 935.

199 *Times Herald*, 730 S.W.2d at 649. Specifically, the court took issue with both the trial court hearing a motion from a non-party (the newspaper) that did not intervene before the trial court’s plenary power expired and with the court of appeals implying that the district court “only lost its plenary power to *alter or change* the judgment and that it still had plenary power to *uphold* the judgment.” *Id.*
Since *Times Herald*, the court has not definitively overruled the case to provide for definitive continuing protective-order modification jurisdiction. This uncertainty is in tension with the court’s approach to post-plenary injunction modifications outside the protective-order context.

Protective orders are similar, in many senses, to prohibitory injunctions—both forbid certain conduct. An injunction could prohibit a wide range of conduct, e.g., the sale or disposal of property or the enforcement of a particular law. At their root, protective orders forbid a specific type of conduct—speech.  

Texas courts have long recognized the power to modify injunctions in light of changed circumstances, even when their plenary power has expired. Any reading of *Times Herald* as an absolute prohibition against post-plenary protective-order modifications (even with evidence of changed circumstances) seems to conflict with the rule that allows courts to modify final injunctions after the ordinary time for doing so has passed.

This conflict may be reason enough to reject *Times Herald* as a limit on protective-order modification. The better approach to modification would allow trial courts to liberally revisit protective orders, even after ordinary jurisdiction has expired. The Texas Supreme Court, however, has not yet explicitly overruled the case in the protective-order context. But Texas Rule of Civil Procedure 76a did create post-judgment jurisdiction for at least a subset of protective and sealing orders. This sliver of jurisdiction has turned out to be quite narrow.

In 1990, the court adopted Texas Rule of Civil Procedure 76a. Rule 76a(7) does create jurisdiction in some protective-order cases. This continuing jurisdiction provision may very well have been, at least in part, a reaction to *Times Herald’s* apparent anti-modification holding. Indeed, one of 76a’s primary proponents expressly recognized that before the adoption of Rule 76a, intervening to modify a protective order after plenary power

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201 See, e.g., City of San Antonio v. Singleton, 858 S.W.2d 411, 412 (Tex. 1993) (“A trial court generally retains jurisdiction to review, open, vacate or modify a permanent injunction upon a showing of changed conditions.”).

202 See TEX. R. CIV. P. 76a.


204 See TEX. R. CIV. P. 76a.

205 See id. 76a(7).
expired “was improper because the court entering the order had lost jurisdiction when the judgment became final.”

At a cursory glance, 76a(7) might automatically provide jurisdiction to modify protective orders to allow sharing in all cases. But the rule actually provides continuing jurisdiction to modify protective orders only in cases involving “court records” as opposed to ordinary unfiled discovery. “Court records” under 76a include filed documents “of any nature” and a subset of unfiled discovery materials that “have a probable adverse effect upon the general public health or safety, or the administration of public office, or the operation of government . . .”

At another quick glance, then, Rule 76a might apply in a case where the allegations in the petition indicate that unfiled discovery information could reveal that the health and safety of thousands of widget-injury victims (to borrow from the hypothetical above) is in jeopardy. This unfiled discovery could, therefore, be considered “court records” subject to Rule 76a. If so, the rule would provide continuing trial-court modification jurisdiction. But one of the supreme court’s seminal Rule 76a decisions has largely narrowed this route to post-plenary protective-order jurisdiction.

In General Tire, Inc. v. Kepple, the court held that trial courts have no self-executing obligation to determine whether unfiled discovery materials are “court records” under Rule 76a. Indeed, where “no party or intervenor contends that the discovery is a ‘court record,’ a trial court need not conduct a hearing or render any findings on that issue.” And Rule 76a’s notice and sealing provisions do not apply to non-court-record discovery.

If Rule 76a’s sealing provisions do not apply, it is unlikely that its continuing jurisdiction provision would apply either. The text of Rule

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207 Id. 76a(7), (9).
208 Id. 76a(2)(c).
210 See id. at 525. This article does not express an opinion on the correctness or wisdom of the Kepple holding.
211 Id.
212 See id.
76a(7) says as much.\textsuperscript{213} Indeed, the rule indicates that a court retains jurisdiction over a “sealing order” (a term typically used to refer to orders sealing court records as opposed to protecting ordinary unfiled discovery).\textsuperscript{214} Another sentence of the same provision establishes the right of a third party to intervene “at any time before or after judgment to seal or unseal court records.”\textsuperscript{215} Nowhere does the rule expressly indicate that trial courts have continuing jurisdiction to modify protective orders restricting access to non-court-record unfiled discovery.\textsuperscript{216}

Likewise, the text of Rule 76a(9) (Application) expressly indicates that Rule 76a does not apply to run-of-the-mill, non-court-record protective orders.\textsuperscript{217} The provision states that “documents in court files not defined as court records by this rule” are subject to “existing law” and not Rule 76a, presumably including its provision for continuing jurisdiction.\textsuperscript{218}

Unfiled discovery is a “court record” under Rule 76a only when a party establishes that it concerns public health or the operation of government.\textsuperscript{219} But in run-of-the-mill protective-order cases (where no party establishes such facts), the text of Rule 76a(7) and 76a(9), along with the court’s decision in \textit{Kepple}, likely eliminates Rule 76a as a source of post-plenary protective-order jurisdiction.\textsuperscript{220}

\textsuperscript{213}See TEX. R. CIV. P. 76a(7). Parties who might seek to obtain continuing jurisdiction over a protective order by filing discovery materials would also be out of luck in Texas. Texas Rule of Civil Procedure 191.4 specifically forbids parties from filing myriad forms of discovery. TEX. R. CIV. P. 191.4 (prohibiting parties from filing documents and tangible things produced in discovery, among other discovery materials).

\textsuperscript{214}TEX. R. CIV. P. 76a(7) (emphasis added).

\textsuperscript{215}Id. (emphasis added).

\textsuperscript{216}Courts would undoubtedly have post-plenary jurisdiction to consider whether unfiled discovery comprises “court records” pursuant to Rule 76a(2)(c) and 76a(7). See TEX. R. CIV. P. 76a(7); \textit{cf} Kepple, 970 S.W.2d at 522–25 (reviewing “court records” determination post-judgment). If unfiled discovery were, indeed, “court records,” courts would also have jurisdiction to modify a protective order (treated as a “sealing” order when court records are involved) restricting dissemination of the material. See TEX. R. CIV. P. 76a(7) (“A court that issues a sealing order retains continuing jurisdiction to enforce, alter, or vacate that order.”).

\textsuperscript{217}See TEX. R. CIV. P. 76a(9).

\textsuperscript{218}See id. The phrasing is curious in the unfiled-discovery context. Unfiled discovery does not reside in “court files” and discovery comprises more types of information than just “documents.”

\textsuperscript{219}See id. 76a(2)(c).

\textsuperscript{220}Even in cases where courts indisputably have jurisdiction (e.g. before final judgment), Texas law arguably gives trial courts broad discretion to strike interventions aimed at modifying protective orders. Indeed, Texas Rule of Civil Procedure 60 allows trial courts to strike an
This potential lack of jurisdiction would seriously hamper discovery sharing in a jurisdiction that simultaneously forbids upfront sharing provisions (in even a subset of protective orders). In many instances, discovery materials that could aid courts and litigants in resolving pending disputes exist in closed cases. If those materials were produced subject to non-sharing protective orders, and if courts have no power to modify those orders, sharing would be impossible. Individual cases may last two years, one year, or even less than a year. The discovery exchanged in those cases, however, may be pertinent to other similar cases for the better part of a decade (or beyond). In a system without upfront discovery sharing provisions in trade secret cases (the system anti-sharing advocates currently demand), the Texas Supreme Court might react in at least one of three significant ways:

1. A categorical upfront sharing ban would force the court to interpret Rule 76a to provide for continuing jurisdiction over all protective orders, including those that do not restrict dissemination of “court records,” contrary to Rule 76a’s plain language and the court’s decision in *Kepple*;

2. An upfront sharing ban would require the court to overrule *Times Herald* expressly and allow liberal post-plenary modification (the court should do this in any event—courts should have post-plenary power to modify protective orders); OR

intervention when it is not “almost essential to effectively protect the intervenor’s interest.” Guar. Fed. Sav. Bank v. Horseshoe Operating Co., 793 S.W.2d 652, 657 (Tex. 1990). This stands in contrast to federal law, where intervening to modify a protective order is liberally allowed under Federal Rule of Civil Procedure 24. See, e.g., San Jose Mercury News, Inc. v. U.S. Dist. Court—N. Dist. (San Jose), 187 F.3d 1096, 1100 (9th Cir. 1999) (“Nonparties seeking access to a judicial record in a civil case may do so by seeking permissive intervention” under Federal Rule of Civil Procedure 24.). A more malleable intervention standard, like the federal approach, is preferable in the protective-order context.

222 The prevalence of “return-or-destroy” provisions in many protective orders would also make sharing through later modification untenable. If parties were required to return or destroy otherwise sharable discovery almost immediately after cases close, post-plenary case-by-case sharing would largely fail. Indeed, parties that no longer possess documents would be unable to share them, protective order modification or not.
3. A sharing prohibition would require the court to amend Rule 329b to provide courts continuing jurisdiction to modify protective orders that do not implicate 76a.

Perhaps the easy answer is simply to continue to allow upfront discovery sharing protective orders—orders that are signed when trial courts undisputedly have jurisdiction to do so.  

IV. DISCOVERY SHARING AND COURT EFFICIENCY

As Garcia v. Peeples recognized, one of the “public policies” favoring shared discovery is increased court efficiency. Courts and commentators around the country have long lauded discovery sharing as a mechanism to avoid wasteful rediscovery of the same information in similar lawsuits. The value of these features is echoed by historical and current discovery-reform efforts.

A. Discovery Sharing’s Relationship with Litigation Efficiency

While there are subtle disagreements as to the proper mechanism to effectuate sharing, virtually no authority categorically opposes the practice. This unanimity flows largely from sharing’s recognized efficiency benefits. The civil rules echo this pro-efficiency sentiment.

Contrary to frequent anti-sharing arguments, e.g., that courts should focus myopically on particular party interests when considering sharing

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223 See Garcia, 734 S.W.2d at 347.
224 Id. at 346–47.
225 See, e.g., Raymond Handling Concepts Corp. v. Superior Court, 45 Cal. Rptr. 2d 885, 887–88 (Cal. Ct. App. 1995) (affirming trial court’s entry of sharing protective order and citing Garcia for the proposition that sharing increases systemic efficiency); Timmins, supra note 22, at 1543 (preferring protective orders with sharing provisions).
226 Compare Richard L. Marcus, Myth and Reality in Protective Order Litigation, 69 CORNELL L. REV. 1, 21–22 (1983) (arguing that collateral litigants should establish entitlement to discovery information before sharing, presumably in an intervention and modification proceeding), with Timmins, supra note 22, at 1543 (preferring protective orders with sharing provisions); see also Benham, supra note 2, at 2192, 2199–2200. But see Campbell, supra note 9, at 784 (opposing discovery sharing).
227 See, e.g., Garcia, 734 S.W.2d at 347.
228 See TEX. R. CIV. P. 1; FED. R. CIV. P. 1.
requests, the rules suggest that courts should actually construe procedural
rules to foster systemic efficiency while furthering the quality of justice.\textsuperscript{229}

For example, Federal Rule of Civil Procedure 1, largely similar to its
Texas counterpart, commands courts and parties to construe and administer
the civil rules to "secure the just, speedy, and inexpensive determination of
every action and proceeding".\textsuperscript{230} Courts' responsibility to secure efficiency
in every case implies that they should account for the systemic impact of
rulings in particular cases. Similarly, Texas Rule of Civil Procedure 1
commands courts to give the rules a "liberal construction" to attain justice
"at the least expense both to the litigants and the state as may be
practicable..."\textsuperscript{231}

Well-crafted discovery-sharing provisions complement Rule 1, making
litigation less costly for the state's courts and litigants on both sides of the
docket.\textsuperscript{232} The efficiencies generated by sharing are relatively
straightforward: Parties in litigation obtain previously produced discovery
materials and thereby avoid wasteful rediscovery in contemporaneous or
subsequent similar cases.

The savings to litigants comes in the form of having to draft fewer
discovery requests, fewer responses to those requests, and fewer motions to
compel responses because much discovery information is already available
from another case.\textsuperscript{233} The savings to the court system flows from not having
to police discovery disputes, a particularly irksome task for trial judges that
is both time consuming and tedious.\textsuperscript{234} Fewer discovery requests mean
fewer disputes over those requests.\textsuperscript{235}

In response to the obvious, commonsense appeal of sharing as a
cost-saving measure, anti-sharing advocates contend that sharing actually
makes litigation less efficient through several clever but flawed
arguments.\textsuperscript{236} For instance, some contend that defendants will stop

\textsuperscript{229}See TEX. R. CIV. P. 1; FED. R. CIV. P. 1.
\textsuperscript{230}FED. R. CIV. P. 1. (emphasis added).
\textsuperscript{231}TEX. R. CIV. P. 1.
\textsuperscript{232}See Benham, supra note 2, at 2216.
\textsuperscript{233}See id.
\textsuperscript{234}Cf., e.g., Brad N. Friedman, Mass Products Liability Litigation: A Proposal for
Dissemination of Discovered Material Covered By a Protective Order, 60 N.Y.U. L. Rev. 1137,
\textsuperscript{235}Cf. id.
\textsuperscript{236}To refute the idea that shared discovery reduces discovery costs, some litigants have cited
an increase in discovery costs since Garcia was decided in 1987. See, e.g., Relator's Brief on the
cooperating in discovery to some extent if subjected to sharing orders. According to this pick-up-my-marbles-and-go-home version of the world, trade secret holders are more likely to fight discovery of trade secrets aggressively unless courts forbid trade secret sharing.

It is less than clear that trade secret holders are generally less cooperative in a sharing system. No one has put forward any empirical data to suggest that discovery disputes are more frequent in courts that allow sharing. And defendants still have substantial incentives to cooperate in discovery, whether sharing is allowed or not. Resisting discovery is costly, and in many cases those costs could exceed the negligible value (if any) of avoiding the risk of inadvertent or intentional sharing protective order violations.

The particular incentives are, of course, dependent on the nature of the sharing provision and the nature of the information at issue. Trial courts would be in the best position to determine whether a particular protective-order provision creates a significant incentive to resist discovery. So instead of a categorical no-sharing approach, those courts should be afforded the discretion to include sharing provisions or not, as appropriate to further case and systemic efficiencies based on the circumstances.

Some have also suggested that a decision forbidding trade secret sharing would have a minimal impact because trade secrets do not comprise a large percentage of discovery information. It is true that trade secret information comprises something substantially less than the whole of discovery information. Evidence of the relative percentage of trade secret

Merits at 42, In re Gen. Motors LLC, 2014 WL 1510890 (Tex. Apr. 16, 2014) (No. 13-0794). This argument ignores what most would acknowledge is a substantial, if not primary, driver of increased discovery costs—the explosion of electronic information subject to discovery. See, e.g., Wright et al., supra note 59, at § 2008.2 (“Electronically stored information can present particularly severe problems” of disproportionate discovery; “One of the consequences of the introduction of the computer has been to increase the amount of information available for a variety of purposes. One of these purposes is responding to discovery. . . .”).

See, e.g., Campbell, supra note 9, at 824 (“Defendants faced with the prospect that documents produced in one case will generate similar claims throughout the country will more aggressively resist disclosure.”).

See, e.g., id.

See Garcia v. Peeples, 734 S.W.2d 343, 345 (Tex. 1987).

See, e.g., Automobile Manufacturers’ Amicus Brief, supra note 3, at 40.

See id.
information in discovery is scant or non-existent. Thus, the true impact of a trade-secret-sharing ban is likely to remain a guess.

And even if the relative percentage of discovery impacted by a no-trade-secret-sharing rule is in fact small, alleged trade secrets are often among the most important information in the case—the designs of an allegedly defective product, for example, or information about potentially safer alternative product designs. Sharing this vital information among similar cases (where its importance likely means it is requested in every case) would obviate the need to wastefully rediscover it.

A no-trade-secret-sharing rule could actually incentivize parties to seek trade secret status for a broader swath of information. And an increase in resource intensive trade secret hearings could significantly increase the cost of discovery. If a trade secret designation came with a guaranteed non-sharing protective order for any information so designated, defendants inclined to resist sharing could very well burden courts with trade secret hearings. On the other side of the docket, plaintiffs interested in sharing would likely contest trade secret status more frequently than they currently do. Trade secret hearings, particularly in complex cases involving terabytes of information, can be lengthy and onerous. Adopting a no-trade-secret-sharing rule would likely result in more of them.

Another argument proceeds that a no-sharing rule would impose minimal costs because parties can already share discovery responses (as opposed to actual discovery information) that identify, but do not include, trade secret data.242 According to this argument, similarly situated litigants could simply request the same data described in the responses and seek to satisfy Rule 507 to the extent trade secrets are at issue.243

This suggestion exposes the devil in the details of the proposal—to obtain the information, a party would have to re-request it and potentially consume additional, unnecessary court time to establish the party is “entitled to access.”244 Under a sharing protective order, on the other hand, parties and courts could skip that discovery fight altogether and simply obtain the materials subject to appropriate disclosure restrictions.

The efficiency gains under a sharing regime would benefit defendants along with plaintiffs. Thus, it is somewhat puzzling that (typically

242 See Relator’s Brief on the Merits, supra note 236, at 43.
243 See id. at 44.
244 See id.
corporate) defendants continue to vigorously resist the practice. These companies contend, with putative earnestness, that they are concerned about protecting trade secrets and that sharing orders do not do enough to protect those secrets.

But these same parties also stand to benefit from a non-sharing regime in other, less savory ways. In a non-sharing system, each plaintiff would be forced to seek the same discovery in virtually identical cases, imposing costs that might otherwise be avoided by sharing and raising the price of entry for legitimate claims.

Indeed, even if a sharing ban were applied just to trade secret information, the cost of bringing some lawsuits might still increase. Assuming trade secret information is sufficiently necessary to be discoverable in one case under Rule 507, other similar cases would presumably need the information as well. Making necessary information available only after parties run and rerun the expensive gauntlet of the discovery process and privilege fights in virtually identical cases is, in effect, a form of claim suppression.

Based on the costs that a categorical non-sharing rule would impose on courts and litigants, the supreme court, and other courts facing similar questions, should affirm Garcia’s commitment to efficiency. In an era with increasing discovery and litigation costs, forbidding sharing in even a subset of cases runs contrary to Rule 1’s laudable goal of making justice more affordable.

B. State and National Efficiency Trends

Texas has a history of rulemaking that complements Rule 1’s command to reduce litigation costs where possible. In 1994, rule-recommending entities created by the supreme court reached a consensus that litigation had

245 See Benham, supra note 2, at 2206 (“In many cases, the putative reason for requesting a nonsharing order—to protect competitive information—may be pretextual.”).
246 See, e.g., Automobile Manufacturers’ Amicus Brief, supra note 3, at 24–29.
247 See Benham, supra note 2, at 2204, 2206.
248 See id.
249 See id.
become too expensive and burdensome.\textsuperscript{252} Justice Hecht (now Chief Justice) expressed his hope for "real restrictions" on discovery.\textsuperscript{253}

The rulemaking process ultimately produced what are now widely known as the 1999 discovery amendments.\textsuperscript{254} The amendments were intended to "curb abuses and reduce cost and delay."\textsuperscript{255} They created a tiered system of presumptive limits on the number of interrogatories, time limits on depositions, and also a limit on the timeframe to complete discovery.\textsuperscript{256} Courts retained the power to adjust the presumptive limits for any case, and parties retained substantial latitude to plead cases out of the most restrictive limits.\textsuperscript{257}

More recent amendments to the Texas civil rules also focus on reducing discovery costs and went further in limiting court and party discretion to opt out of discovery restrictions in some cases.\textsuperscript{258} In 2013, the court adopted Texas Rule of Civil Procedure 169 and amended Rule 190.2, creating an expedited discovery and trial process for smaller cases.\textsuperscript{259} The changes were responsive to the Texas Legislature's request for "rules to promote the prompt, efficient, and cost-effective resolution of civil actions when the amount in controversy does not exceed $100,000."\textsuperscript{260}

Like Texas's efforts, current federal rulemaking aims to make federal discovery efficient.\textsuperscript{261} For more than thirty years, federal discovery practice has been the target of reform efforts.\textsuperscript{262} These changes reflect a belief (by at least some) that discovery in the American pretrial litigation system can be uniquely intrusive and costly, in both time and money.\textsuperscript{263} The costs,
according to these voices, flow from both overbroad discovery requests and unfounded boilerplate objections that consume party resources and court time.264

Over the past few decades, rule amendments have repeatedly targeted federal discovery.265 In 1983, amendments formally introduced the concept that discovery should be “proportional.”266 Later amendments narrowed the scope of discovery from information relevant to the “subject matter of the action” to information relevant to parties’ claims or defenses.267

Most recently, a group of judges, academics, and lawyers convened at Duke Law School in 2010 at the request of the federal Advisory Committee for Civil Rules for a major three-day conference.268 Some at the conference contended that past amendments had not gone far enough in curbing excessive discovery.269

Responding to the Duke Conference concerns, the civil rules advisory committee proposed a package of rule amendments in fall 2013.270 Among other changes, the proposal would promote the proportionality limitation into federal Rule 26(b)(1)’s discovery scope provision.271 Based on this express limitation, lawyers framing discovery requests and courts considering discovery disputes should restrict discovery to that which is

264 See id. at 21.

265 See, e.g., WRIGHT ET AL., supra note 59, at § 2008.1 (describing efforts to constrain the scope and cost of discovery). This Article does not express an opinion on the propriety, wisdom, or potential efficacy of the proportionality amendments.


267 See In re Cooper Tire & Rubber Co., 568 F.3d 1180, 1184 (10th Cir. 2009) (observing 2000 amendment to narrow the scope of discovery).

268 See Marcus, supra note 35, at 17. The conference largely ignored protective-order issues and instead focused on pleading and discovery standards.

269 See id.

270 See id. The Judicial Conference of the United States forwarded a revised version of the proportionality amendment to the Supreme Court for review in April 2015, and the Supreme Court subsequently sent the package of amendments to Congress. See Supreme Court Order, supra note 40; Zoe Tillman, Federal Judiciary Approves Civil Discovery Rules Changes, LEGAL TIMES (Sept. 16, 2014), http://www.law.com/sites/articles/2014/09/16/federal-judiciary-approves-civil-discovery-rules-changes/.

proportional to the case. \textsuperscript{272} In 2015, the United States Supreme Court approved the amendment and forwarded it to Congress. \textsuperscript{273} The proportionality amendment became law in December 2015. \textsuperscript{274}

The rule now sets the scope of discovery to include relevant, non-privileged information in light of "the importance of the issues at stake in the action, the amount in controversy, the parties' relative access to relevant information, the parties' resources, the importance of the discovery in resolving the issues, and whether the burden of the discovery outweighs its likely benefit." \textsuperscript{275}

The debate over proportionality's place in discovery has been heated. A public comment period during spring 2014 produced over 2,300 comments. \textsuperscript{276} To some, the amendments did not go far enough in limiting discovery. \textsuperscript{277} To others, the new limitations will result in a cataclysmic failure of American pretrial litigation. \textsuperscript{278} As with most matters involving public comment by interested lawyers, the truth probably lies in the middle. \textsuperscript{279} But it is possible that the changes will lead to at least some reduction of the amount of discovery information exchanged in federal courts.

Consistent with contemporary federal efforts, Texas has long attempted to control discovery costs, from the supreme court's decision in Garcia, to the 1999 discovery amendments, to the recent expedited trial rules. \textsuperscript{280} Limitations on discovery sharing stand in stark contrast to these efforts. A non-sharing rule in trade secret cases would be a step backward, forcing parties to engage in wasteful, avoidable rediscovery in similar cases and increasing the burden on the system.

\textsuperscript{272} See Marcus, supra note 35, at 20.
\textsuperscript{273} See Supreme Court Order, supra note 40.
\textsuperscript{274} See id.
\textsuperscript{275} FED. R. CIV. P. 26(b)(1).
\textsuperscript{276} See Tera E. Brostoff & Jeffrey D. Koelmay, E-Discovery Rules Gets Late-Night Rewrite, Advisory Committee Approves Rules Package, 82 U.S.L.W. 1549, 1550 (April 14, 2014).
\textsuperscript{277} Cf., e.g., Marcus, supra note 35, at 23–24 ("From the perspective of the rest of the world, this package of changes is likely to seem very modest, perhaps minimal.").
\textsuperscript{278} See Benham, supra note 2, at 2225.
\textsuperscript{279} See id.
\textsuperscript{280} See MCDONALD & CARLSON, supra note 4, at § 13:2; see also ALBRIGHT & HERRING, supra note 251, at § 2:3.
V. CONCLUSION

One of the most curious features of the discovery-sharing fight is that it flips at least some of the players against their traditional positions. Corporate interests and defense lawyers, who typically line up to support pretrial efficiency reforms, lobby against a practice that creates those very efficiencies. In response to this observation, those interests might say that efficiency is not the only important concern in pretrial litigation—protecting proprietary information from undue dissemination to competitors is also important. Sharing, according to these voices, increases the risk of that happening.

But in almost thirty years of sharing in Texas, opponents of the practice have been unable to identify significant problems with attorneys in the sharing class leaking information to competitors or the public at large. The lack of evidence of actual past harm from discovery sharing is deafening in its silence. And it points firmly to another possible motivation: greater savings that might flow from increasing the cost of entry on those who benefit most from discovery sharing. This group includes individuals who claim to have been injured by common products or business practices. While protecting trade secrets in discovery is important, so too is reducing the cost of litigation.

Sharing has few costs and many benefits. Based on the absence of significant evidence that sharing (over a three-decade time period) has deprived anyone of the value of a trade secret, the practice should continue in Texas and beyond.

281 See, e.g., Automobile Manufacturers' Amicus Brief, supra note 3.
282 See, e.g., Campbell, supra note 9, at 824–25 (sharing increases risk of harm to producing parties).
283 See, e.g., Benham, supra note 2, at 2206.
Take a Second-Look at Liquidated Damages in Texas (Regardless of What the Texas Supreme Court Says)

Trey Qualls*

I. INTRODUCTION

The purpose of a liquidated damages clause in a contract is to allow the parties to agree in advance to the amount of compensation due one party in the event of the other party’s breach.¹ Texas courts have long recognized the general enforceability of liquidated damage clauses.² These clauses have become routine in various types of contracts, including real estate sales contracts, construction contracts, and noncompetition agreements to name a few.³ However, as always, the right of contracting parties to make their own bargains is not completely unlimited.⁴ The fundamental goal of the law when it comes to contract damages is to redress breach by compensating the injured party, not to preemptively deter breach by compelling performance.⁵ Therefore, courts will not enforce a liquidated damages provision deemed to function as a “penalty” intended only to secure the performance of the contract.⁶

The determination of whether a provision in a contract is an enforceable liquidated damages clause or an unenforceable penalty is a question of law

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⁵E. Allan Farnsworth, Farnsworth on Contracts § 12.18, at 301 (3d ed. 2004).

for the courts to decide. However, courts have often struggled with articulating and applying consistent standards in making this determination. The distinction between a valid liquidated damages clause and an illegal penalty has been called one of the most subtle questions of the law, leading one New York Court of Appeals judge to comment that “[t]he ablest judges have declared that they felt themselves embarrassed in ascertaining the principle on which the decisions . . . were founded.”

In many jurisdictions, older opinions often make reference to the “intention of the parties” as being the controlling factor. However, commentators have noted these statements can be somewhat misleading. For even in those early decisions, courts regularly acknowledged that “mere use of the term ‘penalty,’ or the term ‘liquidated damages,’ does not determine this intention, if, on the whole, the instrument discloses a different intent.” Thus, the decisions appear to have turned on some criteria other than simply what the parties intended as evidenced by the language in their contracts.

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10 Cotheal v. Talmage, 9 N.Y. 551, 553 (1854); see also Giesecke v. Cullerton, 117 N.E. 777, 778 (Ill. 1917) (“This court has said more than once that no branch of the law is involved in more obscurity by contradictory decisions than whether a sum specified in an agreement to secure performance will be treated as liquidated damages or a penalty . . . .”); Ferguson v. Ferguson, 110 S.W.2d 1016, 1018 (Tex. Civ. App.—Eastland 1937, no writ) (“Whether . . . a sum named in a contract to be paid by a party in default on its breach is to be considered liquidated damages or merely a penalty is one of the most difficult and perplexing inquiries encountered in the construction of written agreements.”) (internal quotation marks omitted).
13 Yetter v. Hudson, 57 Tex. 604, 613 (1882) (internal quotation marks omitted).
14 See Comment, Liquidated Damages and Penalties Under the Uniform Commercial Code and the Common Law: An Economic Analysis of Contract Damages, 72 NW. U. L. REV. 1055, 1062 n.47 (1978) (quoting 11 JOSEPH M. PERILLO, CORBIN ON CONTRACTS § 58.5, at 426 (rev. ed. 2005) (“the intention of the parties is to control, as long as they have the right intention”);
Underlying this purported "intention of the parties" analysis were often two criteria which have become the modern two-part test for analyzing liquidated damages clauses in almost every jurisdiction across the country. The first prong of the test requires that the harm which could be expected to flow from a breach of the contract must be difficult or impossible to estimate. The second requirement is that the amount stipulated as liquidated damages must be a reasonable estimate of just compensation.

At first glance, these two criteria already appear at odds with one another: one based on uncertainty, the other reasonableness. Regarding the first prong, jurisdictions (including Texas) generally agree that the uncertainty of the damages must exist at the time the contract was negotiated and entered into. The second element—often referred to as the more important analysis—is where jurisdictions have differed widely. The reasonableness analysis raises questions such as "reasonable as compared to what?" and "determined as of when?" How a court answers these questions generally places the jurisdiction into one of two camps: those taking a prospective approach to the reasonableness analysis, and those taking a retrospective approach.

Confusingly, Texas courts have at times used language that would seem to place it in both camps. This Note will attempt to briefly describe the differences between the two approaches, trace the history of Texas jurisprudence regarding the reasonableness analysis, and shine a light on

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15 See WILLISTON & LORD, supra note 12, § 65:16, at 291-94; Anderson, supra note 8, at 1086.
17 See Comment, supra note 14, at 1065.
19 See supra note 14, at 1065.
20 WILLISTON & LORD, supra note 12, § 65:17, at 299.
21 See id. at 302.
22 See infra Part III.
23 See infra Part II.
24 See infra Part III.
what appears to be the current Texas approach as applied in the recent Texas Supreme Court decision of FPL Energy LLC v. TXU Portfolio Management Company.25 As that case demonstrates, while Texas courts may use seemingly contradictory language to describe what it is they are doing with regard to the reasonableness analysis, in application their analysis is most consistent with a retroactive or "second-look" approach. Finally, this Note will offer a few basic drafting recommendations for increasing the likelihood that a liquidated damages provision will be enforced in Texas.

II. THE TWO APPROACHES FOR ASSESSING THE REASONABLENESS OF LIQUIDATED DAMAGES

As mentioned above, it is generally well-settled that the uncertainty of damages must be present at the time of contract formation.26 Because few cases have hinged on the uncertainty element,27 the reasonableness of the stipulated damages clause is often decisive. This section provides a basic discussion of the two approaches to the timing of the reasonableness analysis. The purpose is merely to explain the different approaches and their application, not to advocate for one approach over the other. The latter decision is left to the courts.

A. The "Single-Look" Approach

Traditionally, the reasonableness of a liquidated damages clause was judged at the time the contract was made, not the time at which a subsequent breach occurred.28 This approach to reasonableness is sometimes called a "prospective" or "single-look" approach.29 Courts using

25 See infra Part IV.  
26 Oetting v. Flake Unif. & Linen Serv., Inc., 553 S.W.2d 793, 796 (Tex. Civ. App.—Fort Worth 1977, no writ); see Stewart v. Basey, 245 S.W.2d 484, 486 (Tex. 1952); see also Comment, supra note 14, at 1064. While it is worth noting that the uncertainty analysis is also susceptible to the same prospective/retrospective debate as the reasonableness analysis, there appears to be more agreement across jurisdictions that the damages must be difficult to estimate at the time of contract formation. Comment, supra note 14, at 1064. With that said, some commentators have suggested that courts are strongly affected by the facts as of the time of trial and that even for courts proclaiming a prospective approach "what counts is the convenience and efficiency by which actual damages can be measured at trial." Id. at 1065 (emphasis added).  
27 PERILLO, supra note 18, § 58.7, at 440.  
28 FARNSWORTH, supra note 5, § 12.18, at 305–06.  
29 WILLISTON & LORD, supra note 12, § 65:17, at 299–300.
this approach compare the amount of damages stipulated in the contract to the amount of damages that could have reasonably been foreseen or anticipated based solely on what the parties knew at the time of contract formation. As one court applying this approach explained, "[t]he standard of measure here is not furnished by the plaintiff's actual loss or injury . . . but by loss or injury which might reasonably have been anticipated at the time the contract was made . . . . It is the look forward, and not backward, that we are called upon to take . . . ." Under this approach, whether actual damages are greater or less than the amount stipulated in the contract is immaterial. As long as the liquidated sum was a reasonable prediction of the potential damages—as judged at the time the contract was made—courts following this approach will generally enforce the liquidated damages provision.

Courts applying the single-look approach phrase it in a variety of ways. One court has stated that the stipulated amount must bear "a reasonable relation to probable damages and . . . not [be] disproportionate to any damages reasonably to be anticipated." Another has said that the amount in the liquidated damages clause must be a "reasonable estimate of the damages that would actually result if the contract were breached." Regardless of the language used, the court will try to put itself in the same position the parties themselves were in when they were making the contract.

A 1998 Massachusetts appellate court, in reviewing the enforceability of a liquidated damages provision, surveyed the law of every state to determine which test each state applied to the reasonableness analysis. While noting that language and context made precise categorization

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30 See id. at 300.
33 Giuliano v. Cleo, Inc., 995 S.W.2d 88, 99 (Tenn. 1999); see also In re Schaumburg, 97 B.R. at 953 ("parties are not required to make the best estimation of damages, just one that is reasonable").
35 Lawyers Title Ins. Corp. v. Dearborn Title Corp., 939 F. Supp. 611, 616 (N.D. Ill. 1996), aff'd in part, vacated in part on other grounds, 118 F.3d 1157 (7th Cir. 1997).
36 PERILLO, supra note 18, § 58.6, at 431; see also Honey Dew Assocs., Inc. v. M & K Food Corp., 241 F.3d 23, 28 n.3 (1st Cir. 2001) ("a judge, in determining the enforceability of a liquidated damages clause, should examine only the circumstances at contract formation") (internal quotation marks omitted).
difficult, the court found that the single-look approach was most commonly applied, though only by a slight margin. At that time, twenty-two states applied a single-look approach; twenty applied a second-look approach; three were controlled by a statute implicating neither approach; and in the remaining states, the court was not able to discern the approach used. Interestingly, the year after the appellate court in Kelly v. Marx espoused a second-look approach for the state of Massachusetts, the Supreme Judicial Court of Massachusetts reversed course and adopted the single-look approach. Federal courts also appear to apply the single-look test in cases involving federal government contracts.

Courts following the single-look approach cite several advantages to this approach. The most commonly mentioned is the deference it gives to the bargain actually struck by the parties, or what some might call freedom of contract. As Justice Holmes once said in reviewing the enforceability of a liquidated damages clause, "the proper course is to enforce contract[s] according to their plain meaning, and not to undertake to be wiser than the parties . . . ." In testing the validity of a liquidated damages clause only at the time of contracting, the single-look approach arguably "most accurately matches the expectations of the parties, who negotiated a liquidated damage amount that was fair to each side based on their unique concerns and circumstances surrounding the agreement, and their individual estimate of

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38 See id. at 873–74.
39 Id. at 873.
40 Id. at 874; see infra Part II.B for a discussion of the "second-look" approach.
41 Kelly, 694 N.E.2d at 874.
42 Id.
43 Id. at 870.
44 Kelly v. Marx, 705 N.E.2d 1114, 1116 (Mass. 1999) ("The question before us is whether [the] enforceability of a liquidated damages clause is to be tested by analyzing the circumstances at contract formation, the prospective or 'single look' approach, or when the breach occurs, the retrospective or 'second look' approach.... We agree... that a judge, in determining the enforceability of a liquidated damages clause, should examine only the circumstances at contract formation.").
46 See Kelly, 694 N.E.2d at 870; Guiliano v. Cleo, Inc., 995 S.W.2d 88, 100 (Tenn. 1999) ("Generally, the parties to a contract are free to agree upon liquidated damages and upon other terms that may not seem desirable or pleasant to outside observers. In that respect, courts should not interfere in the contract, but should carry out the intentions of the parties and the terms bargained for in the contract, unless those terms violate public policy.") (citations omitted).
damages in event of a breach.”

Related to the idea of freedom of contract, the single-look approach also provides a level of certainty to the parties regarding their potential liability on the contract. Another advantage is that it saves courts, juries, parties, and witnesses the time and expense of having to litigate actual damages after a breach has occurred. Furthermore, courts have noted that in a great number of cases the parties themselves are more intimately acquainted with the peculiar circumstances of the contract or the subject matter of the transaction and are therefore better able to compute the probable damages than are courts or juries. In this sense, the courts recognize the estimate of damages made by the parties themselves “as being the best and most certain mode of ascertaining the actual damage, or what sum will amount to a just compensation.”

The obvious downfall of the single-look approach is the potential windfall it can create if, in the event of breach, actual damages turn out to be much less than a stipulated amount deemed reasonable at the time of contracting. While such disparity may call into question the initial reasonableness of the pre-estimate in the first place, assuming the amount stipulated was reasonable at the time of contracting, a court employing a strict single-look approach would enforce the liquidated damages provision.

The most taxing scenario for the single-look approach is the rare but extreme case where there are no actual damages at all. Some courts stick firmly to the single-look approach and enforce a liquidated damages provision even in light of a subsequent lack of actual damages, the only question being whether the stipulated sum was reasonable when the contract was made. This view weighs the practical advantages of

48 Kelly, 705 N.E.2d at 1117.
49 Giuliano, 995 S.W.2d at 100.
50 Perillo, supra note 18, § 58.7, at 438.
52 Id. at 137–38. For a good article advocating the use of the “single-look” approach, see Dennis R. LaFiura & David S. Sager, Liquidated Damages Provisions and the Case for Routine Enforcement, 20 FRANCHISE L.J. 175 (2001).
54 Farnsworth, supra note 5, § 12.18, at 307.
55 See Sw. Eng’g Co. v. United States, 341 F.2d 998, 1003 (8th Cir. 1965) (“It is not unfair to hold the contractor performing the work to such agreement if by reason of later developments damages prove to be less or nonexistent.”).
upholding a forecast that was reasonable at the time of contracting over the disadvantages of allowing a party who has sustained no actual losses to recover damages.\textsuperscript{57} Other single-look jurisdictions, however, have recognized the distastefulness of such strict adherence and have drawn a somewhat arbitrary line between cases in which there are no actual damages and those in which actual damages simply turn out to be less than anticipated.\textsuperscript{58}

B. The "Second-Look" Approach

The other prevailing method for assessing the reasonableness of a liquidated damages provision compares the stipulated sum in the contract not only to the amount of damages that could reasonably be anticipated at the time of contract formation, but also to the amount of actual damages caused by a subsequent breach of the contract.\textsuperscript{59} This addition of a retrospective analysis from the moment in time of contract breach is often characterized as the "second-look" approach.\textsuperscript{60} The second-look approach is in many ways simply the opposite of the single-look approach. Whereas evidence of actual damages is irrelevant in a true single-look jurisdiction,\textsuperscript{61} courts applying a second-look approach will strike down a liquidated damages provision as an unenforceable penalty if the stipulated sum greatly exceeds the amount of actual damages that later result from a breach.\textsuperscript{62} In that case, the plaintiff’s recovery is limited to the actual damages sustained and proven.\textsuperscript{63} As one court concisely described the process of applying the second-look analysis:

\begin{quote}
[O]ne must first judge whether the provision was a reasonable estimate of difficult-to-ascertain damage at the time the parties agreed to it. If it was a reasonable estimate, one must then conduct a retrospective appraisal of [the] liquidated damages provision. . . . If the actual damages turn out to be easily ascertainable, a court must consider whether the stipulated sum is unreasonably and grossly
\end{quote}

\textsuperscript{57}FARNSWORTH, supra note 5, § 12.18, at 307.
\textsuperscript{58}Id. at 307–08.
\textsuperscript{59}Guiliano v. Cleo, Inc., 995 S.W.2d 88, 99 (Tenn. 1999).
\textsuperscript{60}FARNSWORTH, supra note 5, § 12.18, at 306.
\textsuperscript{61}See, e.g., Frick Co. v. Rubel Corp., 62 F.2d 765, 768 (2d Cir. 1933).
\textsuperscript{62}Guiliano, 995 S.W.2d at 99.
\textsuperscript{63}Id.
disproportionate to the real damages from a breach. If so, the liquidated damages provision will be deemed unenforceable as a penalty, and the court will award the aggrieved party no more than his actual damages.  

Thus, even in a case where the stipulated sum was freely negotiated by the parties and was a reasonable pre-estimate of damages when viewed from the moment of contract formation, under a second-look approach, the provision will not be enforced if actual damages turn out to be substantially lower than the stipulated amount.

Courts adopting the second-look approach often cite to the Uniform Commercial Code and the Restatement (Second) of Contracts for support, both of which are discussed below regarding their application to Texas law. While sometimes referred to as the more “modern” test, as of the 1998 Massachusetts case of Kelly v. Marx mentioned above, the second-look approach was slightly less common than the single-look approach.

The advantages and disadvantages of the second-look approach are largely just the flip-side to those of the single-look approach. The main advantage of the second-look approach is that it prevents the windfalls in favor of the non-breaching party that the single-look approach allows, particularly in cases where there are no actual damages at all. This arguably makes the approach more consistent with the basic principles of contract law—that the aggrieved party should be fully compensated for their losses but that penalty clauses should not be enforced. The biggest criticism of the second-look approach is that it interferes with the parties’ freedom of contract and undermines the certainty they have in their bargains, thus defeating the purpose of stipulating to damages in the first place.

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64 Shallow Brook Assocs. v. Dube, 599 A.2d 132, 137 (N.H. 1991) (second emphasis added) (citations omitted) (internal quotation marks omitted).
65 Id.
67 See infra, Part III.B.
68 PERILLO, supra note 18, § 58.6, at 431.
71 See Anderson, supra note 8, at 1088.
72 See Guiliano v. Cleo, Inc., 995 S.W.2d 88, 100 (Tenn. 1999).
III. HISTORY OF TEXAS JURISPRUDENCE REGARDING THE REASONABLENESS ELEMENT

Putting a finger on Texas’s approach to the reasonableness analysis seems like it should be as easy as simply placing it in either the single-look or the double-look camp. However, a look at the case law reveals that the Texas approach has been less than clear. Different courts have, at times, said different things regarding the appropriate time for assessing the reasonableness of a liquidated damages provision.

Two early Texas cases illustrate the confusion that has plagued the Texas courts on this issue. *Eakin v. Scott* and *Collier v. Betterton* were decided relatively close in time—only seven years apart—and written by the same Texas Supreme Court Justice but have been cited as supporting opposite interpretations of the reasonableness analysis. *Eakin* is an 1888 decision written by Justice Gaines. The case involved a contract for the sale and delivery of cattle from Scott to Eakin for $50,000. The contract called for the first payment of $8,000 to be made by Eakin within sixty days. The contract also included a liquidated damages clause by which Eakin agreed “that the above amount [$8,000] shall act as a forfeiture in the event I shall abandon said trade.” Eakin subsequently breached the contract but refused to pay the $8,000, so Scott sued to recover the stipulated amount. The court in *Eakin* acknowledged that its decision depended “upon the question whether the stipulation for the forfeiture of the $8,000 note is to be treated as an agreement for liquidated damages, or as a mere penalty to recover such damages as the plaintiffs should actually

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73 Indeed, in 1998, the Massachusetts appellate court seemed to have no trouble labeling Texas a “double-look” jurisdiction. *Kelly*, 694 N.E.2d at 874.

74 See *Presnal v. TLL Energy Corp.*, 788 S.W.2d 123, 123 (Tex. App.—Houston [1st Dist.] 1990, writ denied) (“We find that the decisions of the various courts of civil appeals in this state upon this question . . . are hopelessly irreconcilable, and after as full an investigation as we have been able to make of the holdings by our Supreme Court[,] the correct rule to be announced in this case is in considerable doubt . . .”) (quoting *Bourland v. Huffhines*, 244 S.W. 847, 849 (Tex. Civ. App.—Amarillo 1992, writ dism'd w.o.j.)).

75 7 S.W. 777 (Tex. 1888).

76 29 S.W. 467 (Tex. 1895).

77 *Eakin*, 7 S.W. at 777–78.

78 Id. at 778.

79 Id.

80 Id.

81 Id.
Although it was agreed by both sides that no actual damages accrued to Scott as a result of Eakin’s breach, the court upheld the liquidated damages clause “without reference to the actual damages sustained.”

Seven years later, Justice Gaines—now Chief Justice of Texas Supreme Court—wrote the decision in another liquidated damages case, however, this time he sang a different tune. The *Collier* case involved a contract to build a house. The contract provided that if Betterton, the contractor, did not complete construction by October 1, he agreed to pay Collier, the owner, $10 per day for every day thereafter that completion was delayed. Betterton missed the deadline, and Collier was not able to move into the house until November 12. Collier sought liquidated damages for the forty-two days he was delayed in taking possession. Although the liquidated damages award of $10 per day was ultimately upheld, in its rationale the court stated that “[i]f the supposed stipulation greatly exceed the actual loss, if there be no approximation between them, and this be made to appear by the evidence, then, it seems to us, and then only, should the actual damages be the measure of the recovery.” Because Betterton had provided no evidence of the amount of actual damages suffered by Collier, the liquidated damages provision was sustained, and thus the result in *Collier* does not appear all that different from the result in *Eakin*. However, the *Collier* court’s reference to the comparison of actual damages to a stipulated amount represents a marked difference from Justice Gaines’s prior holding in *Eakin* that a liquidated damages provision agreed to by the parties should be enforced “without reference to the actual damages sustained.”

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82 Id.
83 Id. at 778–79.
84 Collier v. Betterton, 29 S.W. 467, 467–68 (Tex. 1895).
85 Id.
86 Id. So called “delay” clauses for liquidated damages are common in construction contracts. See, e.g., Commercial Union Ins. Co. v. La Villa Indep. Sch. Dist., 779 S.W.2d 102, 106 (Tex. App.—Corpus Christi 1989, no writ); Loggins Constr. Co. v. Stephen F. Austin State Univ. Bd. of Regents, 543 S.W.2d 682, 683 (Tex. Civ. App.—Tyler 1976, writ ref’d n.r.e.).
87 Collier, 29 S.W. at 468.
88 Id.
89 Id.
90 Id.
91 Eakin v. Scott, 7 S.W. 777, 779 (Tex. 1888).
LIQUIDATED DAMAGES IN TEXAS

The *Eakin* case appears to have fixed the time for testing the reasonableness of a liquidated damages provision at the time the contract was entered into, disregarding the actual loss sustained.\(^92\) The *Collier* case, on the other hand, held that a liquidated damages provision is only valid so long as there is an approximation between the amount stipulated and the damages actually suffered.\(^93\) In the years following these decisions, Texas courts appeared to endorse one approach or the other based on a desire to either to sustain or strike down the liquidated damages provision in question.\(^94\) This was the state of the law in 1952 when the Texas Supreme Court decided *Stewart v. Basey*,\(^95\) which became—and remains—the style case on liquidated damages in Texas.

### A. Stewart v. Basey and the Common Law Test for Liquidated Damages in Texas.

*Stewart v. Basey* is often cited as establishing the common law test for liquidated damages in Texas.\(^96\) The case involved the breach of a lease contract containing a liquidated damages clause.\(^97\) The lease was for a five-year term, and the rent was $325 per month.\(^98\) A liquidated damages clause

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\(^{93}\) *Id.*

\(^{94}\) *Id.*; see, e.g., Pippin Bros. v. Thompson, 292 S.W. 618, 620 (Tex. Civ. App.—Waco 1927, writ diss’ed w.o.j.) ("Does the amount of damages it can reasonably be inferred the parties had in contemplation at the time of the execution of the contract... bear some reasonable proportion to the amount stipulated?") (emphasis added); Norman v. Vickery, 128 S.W. 452, 453 (Tex. Civ. App.—Dallas 1910, writ ref’d) ("The question is: What did the parties intend at the time the contract was made?") (emphasis added); Whitcomb v. City of Hous., 130 S.W. 215, 218 (Tex. Civ. App.—San Antonio 1910, writ ref’d) (invalidating a liquidated damages clause because the city sustained no actual damages); Cowart v. Walter Connally & Co., 108 S.W. 973, 975 (Tex. Civ. App.—Texarkana 1908, no writ) (holding that the rule announced in *Collier* is "a later expression of the views of the Supreme Court, and we think a better interpretation of the law").

\(^{95}\) 245 S.W.2d 484 (Tex. 1952).


\(^{97}\) *Stewart*, 245 S.W.2d at 485.

\(^{98}\) *Id.*
provided that if the lessee failed to make rental payments when due or breached any other term of the lease, the lease would terminate and the lessee would owe liquidated damages of $150 per month for the remaining months of the unexpired term.\textsuperscript{99} Eleven months into the lease, the lessee vacated the premises and returned his keys to the lessor.\textsuperscript{100} The lessor was able to re-let the premises to other tenants—thus negating any actual damages—but still sought liquidated damages from the breaching tenant in the amount of $150 per month for the remaining months of the original five-year term.\textsuperscript{101}

The Texas Supreme Court rightly identified the controlling question in the case as "whether the language . . . stipulating the damages recoverable for the breach of a lease contract is a provision for liquidated damages or for a penalty."\textsuperscript{102} The court noted that "[v]olumes have been written on the question,"\textsuperscript{103} and it acknowledged the inconsistent judicial decisions on the issue.\textsuperscript{104} In its attempt to reconcile these conflicting lines of authority, the court handed down what became generally recognized as the common law test for liquidated damages in Texas: "All agree that to be enforceable as liquidated damages the damages must be uncertain and the stipulation must be reasonable."\textsuperscript{105} In formulating this test, the court relied on language from the Restatement (First) of Contracts,\textsuperscript{106} which provided that:

(1) An agreement, made in advance of breach, fixing the damages therefor, is not enforceable as a contract and does not affect the damages recoverable for the breach, unless (a) the amount so fixed is a reasonable forecast of just compensation for the harm that is caused by the breach, and (b) the harm that is caused by the breach is one that is incapable or very difficult of accurate estimation.\textsuperscript{107}

Ultimately, the court held that the liquidated damages provision in the lease was not a reasonable forecast of damages because it "provided the

\textsuperscript{99}Id.
\textsuperscript{100}Id.
\textsuperscript{101}Id.
\textsuperscript{102}Id.
\textsuperscript{103}Id.
\textsuperscript{104}Id. at 485–86.
\textsuperscript{105}Id. at 486.
\textsuperscript{106}Id.
\textsuperscript{107}Restatement (First) of Contracts § 339 (Am. Law Inst. 1932).
same reparation for the breach of each and every covenant” without regard for the varying degrees of importance of the different covenants within the lease. Though often credited with establishing the common law test for liquidated damages in Texas, Stewart says nothing about when the reasonableness of a liquidated damages provision is judged or to what extent actual damages are relevant to that determination.

The court did note that “the true test of uncertainty” is “that the damages were very uncertain in the contemplation of the parties when the contract was executed.” One commentator writing soon after the Stewart decision believed this language answered the question for the reasonableness prong as well, and a court of appeals decision just a few years later seemed to support this belief. Texas’s adoption of the Uniform Commercial Code’s (UCC) treatment of liquidated damages a decade later, however, would seem to cast doubt on this interpretation, at least as far as transactions under the Code are concerned.

B. The Uniform Commercial Code and the “Anticipated or Actual Harm” Test

The enactment of Article 2 of the UCC in Texas in 1967 represented a significant departure from the common law test of Stewart for contracts involving the sale of goods. Section 2-718(1) of the Uniform Commercial Code, adopted in Texas as Section 2.718(a) of the Texas Business and Commerce Code, provides that:

Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in light of the anticipated or actual harm caused by the breach,

108 Stewart, 245 S.W.2d at 486–87.
109 Id. at 486.
110 See Mueller, supra note 92, at 756 n.21 (“Although the court stated the time in terms of judging uncertainty, it is clear on a reading of the entire opinion that the same time would apply to the determination of reasonableness.”).
111 See Schepps v. Am. Dist. Tel. Co. of Tex., 286 S.W.2d 684, 690 (Tex. Civ. App.—Dallas 1955, no writ) (“Generally, the question of whether a sum named in a contract...is to be considered as liquidated damages, or merely as a penalty, is...to be determined as of the time when the contract was executed. The viewpoint of the parties at the time when the contract was made, and not the situation which is shown to have existed when it was breached, is to be considered in determining the issue as to reasonableness of the stipulation or certainty as to actual damages.”) (citations omitted) (internal quotation marks omitted).
112 TEX. BUS. & COM. CODE ANN. § 2.718(a) (West 2009).
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.\[^{113}\]

While seemingly incorporating both the uncertainty and reasonableness prongs of the common law test, the most significant change is the UCC’s specific inclusion of “actual damages” in the determination of reasonableness. Thus, the “anticipated or actual harm” test would appear, at least at first glance, to be most consistent with a second-look approach. As some commentators have pointed out, however, the “anticipated or actual harm” language is actually subject to multiple interpretations.\[^{114}\]

There is no debating that the UCC makes actual damages now relevant to the reasonableness determination in contracts for the sale of goods. The question is what role actual damages should play. Does the “anticipated or actual harm” language require that a liquidated damages provision be reasonable when compared with *either* anticipated or actual harm?\[^{115}\] Or should the “or” be read as an “and,” and thus a stipulated amount must be reasonable when compared to both anticipated and actual damages?\[^{116}\]

When the test is read literally—in the disjunctive in which it was written—a liquidated damages provision need only be reasonable when compared to one or the other of anticipated harm or actual harm.\[^{117}\] As applied by one court approving of this interpretation, anticipated harm and actual harm would be treated as two alternative means for validating a liquidated damages provision.\[^{118}\]

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\[^{113}\] U.C.C. § 2-718(1) (AM. LAW INST. & UNIF. LAW COMM’N 2011).

\[^{114}\] See, e.g., Comment, supra note 14, at 1070; Anderson, supra note 8, at 1099; Margaret L. Hussey, Comment, Liquidated Damages: A New Rule for Texas Under the Uniform Commercial Code?, 32 BAYLOR L. REV. 123, 128 (1980).

\[^{115}\] See Comment, supra note 14, at 1070–71.

\[^{116}\] Id.

\[^{117}\] See Anderson, supra note 8, at 1093–94.

\[^{118}\] Equitable Lumber Corp. v. IPA Land Dev. Corp., 344 N.E.2d 391, 395 (N.Y. 1976) (“a liquidated damages provision will be valid if reasonable with respect to [e]ither (1) the harm which the parties anticipate will result from the breach at the time of contracting or (2) the actual damages suffered by the nondefaulting party at the time of [the] breach”); see also Cal. & Hawaiian Sugar Co. v. Sun Ship, Inc., 794 F.2d 1433, 1436 (9th Cir. 1986), amended by 811 F.2d 1264 (9th Cir. 1987) (“The choice of the disjunctive appears to be deliberate.”); Anderson, supra note 8, at 1098 (“Although section 2-718 does refer to actual harm, the reference is in the disjunctive and, therefore, can be read to exclude evidence of actual harm if the clause is found to
A second interpretation of the UCC’s “anticipated or actual harm” language is more in line with a second-look approach to reasonableness, where a provision that appeared reasonable at the moment of contract formation—i.e. in relation to “anticipated harm”—could still be held to be an unenforceable penalty if it is not also reasonable when compared with the actual harm that resulted from a breach.\(^{119}\) It is somewhat misleading to characterize this interpretation as requiring that the stipulated amount be reasonable when compared to both anticipated and actual harm because there would be no practical reason for invalidating a liquidated damages clause that accurately approximates actual damages but not anticipated harm.\(^{120}\) Therefore, in practice, this approach only cares whether the stipulated amount is reasonable when compared to actual damages, which reflects a true second-look approach to reasonableness.

Another question raised by the language of the UCC is what effect to give the last sentence of Section 2-718(1), which states: “A term fixing unreasonably large liquidated damages is void as a penalty.”\(^{121}\) This sentence can be read as either placing an additional restriction on liquidated damages, or as merely explaining the consequence for failing to satisfy the “anticipated or actual harm” analysis in the first sentence.\(^{122}\) New York appears to be the lone state interpreting this sentence as a separate test to be applied independently of the criteria in the first sentence of Section 2-718(1).\(^{123}\) This sentence is more accurately read as merely clarifying the penalty imposed once a liquidated amount is found to be unreasonable under the “anticipated or actual harm” test of the first sentence.\(^{124}\) Indeed, reading the last sentence as an additional test by which a liquidated

\(^{119}\) See Anderson, supra note 8, at 1099.

\(^{120}\) Id. (“there would be no sense in striking down such a clause, because that would leave the court in a position requiring it to determine damages under usual legal tests, which would bring it to the same dollar amount as the liquidated clause”).

\(^{121}\) U.C.C. § 2-718(1) (AM. LAW INST. & UNIF. LAW COMM’N 2011); TEX. BUS. & COM. CODE ANN. § 2.718(a) (West 2009).

\(^{122}\) Hussey, supra note 114, at 128.

\(^{123}\) See, e.g., N. Bloom & Son (Antiques) Ltd. v. Skelly, 673 F. Supp. 1260, 1268 (S.D.N.Y. 1987) (“The second sentence of § 2-718(1) is held to constitute a separate test . . . .”); Equitable Lumber, 344 N.E.2d at 395 (“Having satisfied the test set forth in the first part of subdivision (1) of section 2-718, a liquidated damages provision may nonetheless be invalidated under the last sentence of the section if it is so unreasonably large that it serves as a penalty . . . .”).

\(^{124}\) See Hussey, supra note 114, at 128; see also Anderson, supra note 8, at 1105–06.
damages clause could be invalidated would only seem plausible under the second-look approach described above; for if a stipulated damages provision could satisfy the "either/or" test based on its reasonable relation to anticipated damages only to be struck down by the last sentence of Section 2-718(1) for being "unreasonably large," it would seem to invalidate the "either/or" interpretation of the test altogether. Interestingly, this sentence was completely removed from Section 2-718(1) when Article 2 of the UCC was revised in 2003. However, because no state chose to adopt the 2003 amendments, they were withdrawn from the Code in 2011 and thus the sentence remains in Section 2-718(1).

1. The "Equivocation" of the Restatement (Second) of Contracts

Section 356 of the Restatement (Second) of Contracts, published in 1981, was drafted to "harmonize with Uniform Commercial Code Section 2-718(1)," and provides the following:

Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in the light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty.

Upon initial inspection, the language of the Restatement (Second) appears to track very closely to the UCC. The Restatement echoes the "anticipated or actual" harm test of the UCC—though it replaces "harm" with "loss"—and, indeed, the Restatement (Second) is often cited as persuasive authority in support of a second-look approach to reasonableness.

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125 See Anderson, supra note 8, at 1106. Paradoxically, this is exactly what the New York Court of Appeals did in Equitable Lumber when it held that a liquidated damages provision could satisfy the first sentence of § 2-718(1) and yet still be struck down for being "unreasonably large" per the second sentence. 344 N.E.2d at 395–97.

126 U.C.C. § 2-718(1) (as amended in 2003). The reasons provided in the Official Comments were that it was unnecessary, misleading, and redundant. Id. cmt. 3.


129 Id. § 356(1).

However, in the comments to Section 356, the Restatement provides the following: “Furthermore, the amount fixed is reasonable to the extent that it approximates the loss anticipated at the time of the making of the contract, even though it may not approximate the actual loss.” The comment then directs the reader to the following illustration:

A contracts to build a grandstand for B’s race track for $1,000,000 by a specified date and to pay $1,000 a day for every day’s delay in completing it. A delays completion for ten days. If $1,000 is not unreasonable in light of the anticipated loss and the actual loss to B is difficult to prove, A’s promise is not a term providing for a penalty and its enforcement is not precluded on grounds of public policy.

This comment and illustration seem surprisingly to reflect a single-look approach to reasonableness.

The next illustration uses the same fact pattern as the previous illustration but changes it slightly to address the situation in which there are no actual damages:

The facts being otherwise as stated in [the previous illustration], B is delayed for a month in obtaining permission to operate his race track so that it is certain that A’s delay of ten days caused him no loss at all. Since the actual loss to B is not difficult to prove, A’s promise is a term providing for a penalty and is unenforceable on grounds of public policy.

The situation not addressed by the Restatement, however, is the one that falls just between these two illustrations—the one in which the liquidated damages provision is reasonable when compared to anticipated damages but where actual damages can be readily proven to be much lower than the amount stipulated. Thus, as one commentator noted, the Restatement “equivocates” on the most difficult liquidated damages situation.

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132 Id. § 356 cmt. b, illus. 3.
133 Id. § 356 cmt. b, illus. 4.
134 Anderson, supra note 8, at 1093.
135 Id.
C. Post-UCC Caselaw in Texas

The additional confusion created by the "anticipated or actual harm" language in the UCC—and repeated in the Restatement (Second) of Contracts—has not been lost on Texas courts. The question of whether Texas follows the traditional single-look or the modern second-look approach to reasonableness has continued to stymie the intermediate appellate courts, and cases citing both approaches can still be found since the enactment of the UCC in Texas. Adding to the confusion, a new breed of cases sprang up in the wake of the UCC and the Restatement in which the courts use language that would seem to support both approaches within a single decision. The following two cases represent this post-UCC trend.

1. Muddying the Water

The facts of Baker v. International Record Syndicate are good facts for a liquidated damages clause. Baker was a photographer hired by International Record Syndicate to photograph a little-known musical

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137 To be fair, the federal courts have not fared much better at nailing down the Texas approach. See, e.g., Advance Tank & Constr. Co. v. City of DeSoto, 737 F. Supp. 383, 385 (N.D. Tex. 1990) (citing Stewart v. Basey for the proposition that "a liquidated damages provision is to be considered in light of the circumstances as the parties perceived them at the formation of the contract, and not as they exist when the contract was performed (or breached) and the damages occurred"). But see Thanksgiving Tower Partners v. Anros Thanksgiving Partners, 64 F.3d 227, 232 (5th Cir. 1995) (stating that under Texas law "liquidated damages must not be disproportionate to actual damages as measured at the time of the breach" and that "if the liquidated damages are disproportionate to the actual damages, the clause will not be enforced and recovery will be limited to the actual damages proven").

138 See, e.g., Nexstar Broad., Inc. v. Gray, No. 09-07-364 CV, 2008 WL 2521967, at *3 (Tex. App.—Beaumont June 26, 2008, no pet.) ("Evidence that the harm caused is difficult to estimate, and that the amount of liquidated damages is a reasonable forecast, must be viewed as of the time the parties executed the contract."); Murphy v. Cintas Corp., 923 S.W.2d 663, 666-67 (Tex. App.—Tyler 1996, writ denied) (holding a liquidated damages provision to be enforceable even though actual damages were readily calculable at the time of trial); Guido & Guido, Inc. v. Culberson Cty., 459 S.W.2d 674, 678 (Tex. Civ. App.—El Paso 1970, writ ref'd n.r.e.) ("The amount of actual damages is relevant to the issue of whether the stipulation for damages is reasonable, for it must be so in order to be enforced and must bear a reasonable relationship to the actual damages contemplated or, in fact, suffered as a result of the breach.").

139 Baker, 812 S.W.2d at 53.
Baker mailed thirty-seven negatives to the record company, but when the negatives were returned to Baker they had holes punched in them. The contract between Baker and the record company provided for liquidated damages of up to $1,500 per photograph if any photographs were lost or damaged by the record company. On appeal, the court noted that Baker had presented evidence at trial of the wide range he had been paid for similar photographs in the past, demonstrating both the difficulty of estimating the true value of the photographs as well as the reasonableness of the $1,500 per photograph estimate. Therefore, based on the band’s unknown potential for fame at the time, the inherent difficulty of valuing a piece of art in general, and the broad range of values and long-term earning power of photographs, the court found that $1,500 per photograph was not an unreasonable estimate of damages.

The result in Baker seems to be the correct one. This was clearly a situation where the actual damages that could be expected to flow from a breach of the contract would be very difficult to determine at the time of contracting, and there was evidence presented at trial to support the $1,500 per photograph estimate. But the confusing aspect of Baker is not in the result; it is in the reasoning—or rather the language—employed by the court in reaching the result.

After quoting the UCC rule, as codified in the Texas Business and Commerce Code, the court restated the rule using the language of the two-part, common law test of Stewart. The court noted this rule “might be termed the ‘anticipated harm’ test.” Even more definitively, the court explicitly stated that “[e]vidence related to the difficulty of estimation and the reasonable forecast must be viewed as of the time the contract was

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140 Id. at 54–55.
141 Id.
142 Id.
143 Id. at 55 (noting he had made as little as $125 and as much as $1,500 off of a single photograph).
144 Id. at 55–56.
145 Id. at 55.
146 Id.; see supra, Part III.B.
147 Baker, 812 S.W.2d at 55 (“Under Texas law, a liquidated damages provision will be enforced when the court finds (1) the harm caused by the breach is incapable or difficult of estimation, and (2) the amount of liquidated damages is a reasonable forecast of just compensation.”).
148 Id.
executed." Only a few lines later, however, the court provided that "[a]ditionally, liquidated damages must not be disproportionate to actual damages," and that "[i]f the liquidated damages are shown to be disproportionate to the actual damages, then the liquidated damages can be declared a penalty and recovery limited to actual damages proven." This, the court noted, "might be called the 'actual harm' test."

Ultimately, the court's intermingling of prospective (single-look) language with retrospective (second-look) language did not affect the result in that case because, on these facts, the actual damages were just as difficult to determine at the time of trial as they had been at the time of contracting. The question not answered by these facts is the same question on which the Restatement "equivocates": what if the estimate was reasonable at the time of contracting but actual damages have become susceptible to calculation by the time of trial and are much less than the stipulated amount?

2. Preparing a Path to the Texas Supreme Court

A recent case out of the Fourteenth Court of Appeals in Houston looked squarely at the relationship between the common law and statutory tests for liquidated damages and decided that they are, in fact, the same test and that both are consistent with a second-look approach to reasonableness. The Garden Ridge case involved the retail housewares chain, Garden Ridge, and one of its vendors, Advance. Garden Ridge placed an order with Advance for 4,450 inflatable snowmen of different sizes, which it planned to sell during the holiday season. Shortly before putting the snowmen out for sale, Garden Ridge realized that some of the snowmen in the shipment did not conform to the purchase order it had submitted to Advance. Garden Ridge decided to sell the snowmen anyway but then charged back to Advance the entire purchase price for all of the snowmen pursuant to a

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149 Id. (emphasis added).
150 Id.
151 Id.
152 Id. at 55-56.
154 Id. at 435.
155 Id.
156 Id.
liquidated damages clause in its vendor contract addressing "unauthorized substitution" of merchandise. At trial, Garden Ridge did not establish any amount of actual damages from Advance’s noncompliance with the purchase order.

Reviewing whether the liquidated damages provision in the vendor contract was enforceable, the appellate court first noted that the UCC test and the common law test for liquidated damages “reflect the same essential factors and the same type of reasonableness test.” The court equated the first clause of § 2.718(a) (requiring that the liquidated damages be “reasonable in light of the anticipated or actual harm caused by the breach”) with the common law requirement that liquidated damages be a “reasonable forecast of just compensation.” It equated the second and third clauses of § 2.718(a) (regarding “the difficulties of proof of loss”) with the common law requirement “that the harm caused by the breach is incapable or difficult of estimation.”

Having established that the tests are the same, the court turned to Garden Ridge’s argument for an “ex ante” reasonableness analysis. While acknowledging that language in Baker would seem to support Garden Ridge’s single-look theory, the court went on to hold that unreasonableness can be established by showing that actual damages are much less than the amount stipulated in the contract. Thus, basing its decision on the explicit reference to “actual harm” in the UCC, the court applied a second-look approach and found that the liquidated damages clause was unenforceable because there were no actual damages.

A concurring opinion, however, argued that the statutory rule is actually different from and thus supersedes the common law rule in contracts for the sale of goods. The concurring judge felt the majority’s interpretation of the UCC’s language—specifically the word “or”—strained the plain

157 Id. at 435–36.
158 Id. at 436.
159 Id. at 439.
160 Id. at 438.
161 Id.
162 Id. at 439 (“That is, if, at the time the contract is formed, actual damages are difficult to estimate and the amount specified in the contract is a reasonable forecast of just compensation, a liquidated damages term is enforceable.”) (emphasis added).
163 Id. at 440.
164 Id.
165 Id. at 447 (Frost, J., concurring) (citation omitted).
meaning of the statute and undermined the freedom of contract.\textsuperscript{166} Following the "either/or" interpretation of the UCC discussed above,\textsuperscript{167} the judge argued that "a liquidated-damages provision may be reasonable based upon either anticipated harm or actual harm caused by the breach."\textsuperscript{168} Thus, the party asserting penalty should have to show "unreasonableness under both anticipated harm and actual harm caused by the breach."\textsuperscript{169} This judge noted "there are now three different and conflicting views on this question from the three intermediate appellate courts that have addressed this issue,"\textsuperscript{170} but expressed hope that the Texas Supreme Court would clarify Texas’s position in one of the cases in which the court had recently granted review.\textsuperscript{171} That case was \textit{FPL Energy LLC v. TXU Portfolio Management Co.},\textsuperscript{172} discussed below.

\section*{IV. The Texas Supreme Court "Clarifies" Its Position on Reasonableness}

As noted in the concurrence to \textit{Garden Ridge}, the \textit{TXU} case provided the Texas Supreme Court with an opportunity to settle once and for all the question of whether Texas is a single-look or a second-look jurisdiction.\textsuperscript{173}

\subsection*{A. Facts}

The facts of the case are somewhat complicated. The case involves a liquidated damages provision in a contract for the production of electricity and renewable energy credits.\textsuperscript{174} The plaintiff, TXU, was a retail electricity provider distributing electricity directly to consumers.\textsuperscript{175} Beginning in 1999, Texas energy providers, like TXU, were required to purchase a certain portion of the electricity they distribute from renewable sources.\textsuperscript{176} At the same time, the legislature also created a renewable energy credit

\begin{footnotesize}
\begin{enumerate}
\item \textit{Garden Ridge}, 403 S.W.3d at 448 (Frost, J., concurring).
\item \textit{Garden Ridge}, 403 S.W.3d at 450 (Frost, J., concurring).
\item \textit{TXU}, 426 S.W.3d at 60–61.
\item \textit{Id.} at 61.
\end{enumerate}
\end{footnotesize}
(REC) trading program, whereby distributors like TXU could purchase RECs in lieu of purchasing actual capacity from renewable sources. One REC represents one megawatt hour of energy produced from renewable sources. The producers of renewable energy, therefore, can sell both the actual renewable energy produced, as well as the RECs created by that production.

FPL was a renewable energy production company operating several windfarms. In 2000, TXU contracted with FPL to purchase renewable electric energy, as well as the RECs generated from the production of that energy, in order to meet TXU’s statutory renewable energy requirements. In the event that FPL failed to meet its obligations under the contract, the contract provided for liquidated damages of $50 per REC not produced. This $50 per REC figure was tied to the penalty TXU would be assessed by the Texas Public Utilities Commission for failing to meet its REC requirement. The contract also provided that if the Public Utilities Commission ever removed or amended the $50 per REC penalty, the liquidated damages under the contract would be equal to the lesser of (1) the amended penalty or (2) twice the annual average market price per REC as determined by the Public Utilities Commission. For several years, FPL failed to provide the agreed upon amount of renewable energy and RECs to TXU.

B. Procedure

TXU sued FPL for breach of contract and sought liquidated damages for FPL’s failure to provide the agreed upon RECs and electricity. The trial court refused to enforce the liquidated damages provision because TXU was able to cover by obtaining substitute electricity elsewhere and because it determined that the stipulated amount of $50 per REC was not a realistic price for the substitute electricity.

177 Id.
178 Id.
179 Id.
180 Id.
181 Id.
182 Id. at 66.
183 Id.
184 Id.
185 Id. at 62.
186 Id.
forecast of damages. The court of appeals, however, held that the liquidated damages provision was enforceable because the damages were difficult to estimate and the $50 per REC was a reasonable estimate of just compensation; thus, it assessed damages at $29 million based on a deficiency of 580,000 RECs and a deficiency rate of $50 per REC.

C. Analysis

For reasons not related to this Note, the Texas Supreme Court held, as a preliminary matter, that the liquidated damages provision could be applied only, if at all, to REC deficiencies (not failure to deliver actual renewable electricity capacity), and only to those REC deficiencies not excused by lack of transmission capacity or curtailment orders from the Electricity Reliability Council of Texas. Thus, the appellate court's damages assessment of $29 million was immediately cut down to a possible $11 million based on a 220,000 REC deficiency that was determined to be directly attributable to FPL.

The court then considered the enforceability of the liquidated damages provision with regard to those 220,000 RECs. After affirming that "[t]he basic principle underlying contract damages is compensation for losses sustained and no more," the court restated the "two indispensable findings a court must make to enforce contractual damages provisions: (1) the harm caused by the breach is incapable or difficult of estimation, and (2) the amount of liquidated damages called for is a reasonable forecast of just compensation."

Next, the court paid lip service to the traditional, single-look approach by stating: "We evaluate both prongs of this test from the perspective of the parties at the time of contracting." And then, like so
many courts before it, in the very next sentence the court stated that "a liquidated damages provision may be unreasonable because the actual damages incurred were much less than the amount contracted for."\(^{194}\)

Regarding the first element of the test for liquidated damages, the court agreed with TXU that damages for failure to provide the agreed upon RECs were difficult to estimate at the time of contract formation.\(^{195}\) The court reached this conclusion based on the uncertain market for RECs at the time of contracting.\(^{196}\) The statutory scheme was passed in 1999; at the time of contracting in 2000, the market for RECs did not yet exist.\(^{197}\)

Moving on to the second element of the test, the court addressed what it termed the "unbridgeable discrepancy" between the liquidated damages provision as written and the "unfortunate reality in application."\(^{198}\) The liquidated damages provision as written provided for liquidated damages of $50 per REC, or if the statutory penalty applicable to TXU were ever amended, then the lesser of (1) the amended amount or (2) twice the annual average market price per REC as determined by the Public Utilities Commission.\(^{199}\) Because the statutory penalty had not been amended, and because the Public Utilities Commission had not issued a determination of the average annual market price per REC, applying the liquidated damages provision as written would have resulted in liquidated damages of $50 per REC.\(^{200}\) The court, however, ignoring the language which required the determination of market value to come from the Public Utilities Commission, stated that "[t]he contracts ... anticipate that the amount of damages may be tied to market value, rather than an arbitrary number."\(^{201}\)

Although the Public Utilities Commission had expressly denied TXU’s request to issue a determination of the annual average market price per REC, the court noted that the actual market value of a REC during the period in question ranged from $4 to $14.\(^{202}\) Thus, the court indicated that

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\(^{194}\) TXU, 426 S.W.3d at 70. (internal quotation marks omitted).
\(^{195}\) Id.
\(^{196}\) Id.
\(^{197}\) Id.
\(^{198}\) Id. at 72.
\(^{199}\) Id.
\(^{200}\) Id.
\(^{201}\) Id. at 71.
\(^{202}\) Id. at 72.
the appropriate amount of damages should be between $8 and $28 per REC, “depending on what the PUC would have determined as the actual market value of a REC in each year.” This would have placed TXU’s damages somewhere between $1,760,000 and $6,160,000.

Ultimately, because the court found that actual damages, whatever they might have been found to be by the Public Utilities Commission, would have been less than the stipulated amount of $50 per REC, the court held that the liquidated damages clause was an unenforceable penalty. While the court noted that the law does not “create a broad power to retroactively invalidate liquidated damages provisions that appear reasonable as written,” it stated that the forecast of damages in this case “was flawed by its reliance on events that did not and perhaps [could not] occur.”

D. Implications of TXU

1. What the Texas Supreme Court Held

Whatever its language in getting there, the Texas Supreme Court appears to have interpreted the common law test for liquidated damages to apply a second-look approach to reasonableness, one in which actual damages can retrospectively invalidate a provision even if that provision was reasonable when viewed from the moment of contract formation.

2. What the Texas Supreme Court Did Not Hold

Contrary to what it may appear, the Texas Supreme Court did not address the question before the court in Garden Ridge regarding whether the language of the UCC should be interpreted to require only that liquidated damages be reasonable when compared to either anticipated or actual harm. The Texas Supreme Court, noticeably, did not mention the UCC in its holding in TXU because the UCC is only applicable to transactions in “goods,” and the transmission of electrical power has previously been determined by the court not to be a “good” for purposes of

201 Id.
204 See id.
205 Id.
206 Id. (referring to a Public Utilities Commission determination of the market value of RECs during the applicable period).
207 See id.
the UCC. Until this specific question is addressed by the Texas Supreme Court, it is still an open question; however, based on the results of Baker and Garden Ridge, and by analogy the court’s application of a second-look approach under the common law test in TXU, it seems safe to assume that the court would likely place emphasis on actual damages in cases under the UCC as well.

V. DRAFTING RECOMMENDATIONS

As the saying goes, hindsight is twenty-twenty. Or, in the context of liquidated damages, what was reasonable at one point in time may have become unreasonable in retrospect. Thus, it seems that even the most carefully drafted liquidated damages provision may be invalidated as a penalty if actual damages wind up being less than was reasonably anticipated at the time of contracting. There is no precise formula by which to determine when liquidated damages become disproportionate to the actual damages; therefore, the best one can do is try to make sure liquidated damages are reasonable at the time of contracting. With that said, what follows are some general recommendations for drafting liquidated damages clauses in Texas.

A. Call It “Liquidated Damages”

Courts have routinely held that merely designating a clause in a contract as “liquidated damages” will not prevent the courts from holding that it is in fact a penalty, and vice versa. However, there is no sense in inviting controversy. Therefore, when drafting a liquidated damages provision, avoid using the term “penalty,” and instead specifically refer to the provision as “liquidated damages.”

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212FARNSWORTH, supra note 5, § 12.18, at 319.
B. Include Explicit “Recitals”

It may be beneficial to include explicit recitals in the contract acknowledging that “actual damages are uncertain and would be difficult of ascertainment,” and that both parties agree the stipulated sum “constitutes reasonable compensation in the event of a breach.”213 One example, in the context of a contract for the sale of real estate, might include the following:

The parties to this contract agree that the Seller’s actual damages, in the event of a default by the Purchaser, would be difficult of definite ascertainment because of the uncertainties of the real estate market and the fluctuations of property values between the date of this contract and the date of breach, and because of differences of opinion with respect thereto, and the parties therefore agree that such amount is, as to each of them, reasonable as liquidated damages.214

Parties may also want to clearly express that the stipulated sum is intended as “liquidated damages and not as a penalty,” and that it is meant to be “compensatory” rather than “punitive.”215

Finally, it may be wise to recite a nonexhaustive list of the general categories of losses which are intended to be compensated by the liquidated damages clause.216 If nothing else, this may serve as evidence of the types of damages that were “anticipated” by the parties at the moment of contract formation. It also has the added benefit of providing evidence of foreseeability for consequential damages in the event that liquidated damages are not enforced.217

C. Avoid “Shotgun” Clauses

Courts have historically invalidated liquidated damages clauses that prescribe the same amount of liquidated damages for breaches of varying degrees of importance.218 This type of clause is sometimes referred to as a

214 Id. at § 55.293[2].
215 Id. at § 55.293[1][a].
216 Farnsworth, supra note 5, § 12.18a, at 320.
217 Id.
218 See, e.g., Stewart v. Basey, 245 S.W.2d 484, 486–87 (Tex. 1952).
"shotgun" or "blunderbuss" clause. Instead, liquidated damages clauses should be drafted narrowly so that the stipulated sum relates to a particular, specific type of breach. Alternatively, a clause in which damages are graduated based on some formula or criteria that take into account the potential for the varying degrees of seriousness of the breach may be more likely to be enforced.

D. Avoid "Multiples" of Actual Damages

Liquidated damages clauses providing for some multiple of actual damages have been held to be illegal as a matter of law in Texas. The definitive case on this is the Texas Supreme Court case of Phillips v. Phillips, in which a partnership agreement between ex-spouses provided for liquidated damages of ten times actual damages in the event of a breach of the partnership agreement.

E. Avoid "Damages-Plus" Clauses

Similar to the "multiples" clauses mentioned above, parties should never draft a liquidated damages clause that attempts to allow the aggrieved party to collect some level of liquidated damages in addition to actual damages. This sort of clause has been described as attempting to allow the aggrieved party to "have his cake and eat it too," and such a clause could never logically be supported as being a reasonable forecast of damages.

F. Consider a Choice of Law Provision

A drafter in a second-look jurisdiction wishing to take advantage of the certainty the single-look approach provides may wish to include a choice of law provision directing that the relationship between the parties be controlled by the law of a state following the single-look approach to

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219 Farnsworth, supra note 5, § 12.18a, at 319.
220 Anderson, supra note 8, at 1110.
221 Id. at 1109–10; Farnsworth, supra note 5, § 12.18a, at 319.
223 Id. at 786–87.
224 Anderson, supra note 8, at 1110.
225 Id.
226 Farnsworth, supra note 5, § 12.18a, at 319.
reasonableness. Note, however, that the forum state may still choose not to apply the law of the chosen state, notwithstanding the choice of law provision, if doing so would violate the public policy of the forum state.  

G. Consider a Bonus for Early Performance as an Alternative to Liquidated Damages.

An alternative to a liquidated damages clause may be to offer a bonus or premium for early performance. For example, where a $1,000 per day penalty for delayed performance may be unenforceable, moving the completion date in the contract to 10 days later but then offering a $1,000 per day bonus for each day the work is finished early may be allowable. Obviously, adjustments for deadlines and contract price must be taken into consideration. While this sort of clause may still be subject to the same penalty analysis as a liquidated damages provision, courts may be understandably hesitant about where to draw the line in this area.

H. Other Considerations

Given the second-look approach applied by the Texas Supreme Court in TXU, it may go without saying that a forecast of damages has a better chance of being viewed as reasonable if there is, in fact, some level of actual damages proven. Plaintiffs with no actual damages have lost the ability in Texas to hide behind a liquidated damages clause that appeared reasonable at the outset. Even actual damages that are smaller than expected stand a better chance of being reasonable compared to a stipulated amount than no damages at all. Thus, if a defendant can prove, or if a plaintiff concedes, that no actual damages occurred, even a reasonable pre-estimate will likely not be enforced. Note the difference between a lack of actual damages and a situation in which actual damages exist but remain incapable or very difficult to quantify after a breach, as was the case in Baker. On a related note, there is some support for the idea that the more difficult it

228 FARNSWORTH, supra note 5, § 12.18, at 315.
229 Id.
230 Id.
would be to estimate damages, the more lenient a court might be in assessing the reasonableness of the estimation.\(^{233}\)

VI. CONCLUSIONS

In stating that reasonableness is assessed “from the perspective of the parties at the time of contracting” but then striking down the liquidated damages provision as an unenforceable penalty based on the “unbridgeable discrepancy between [the provision] as written and the unfortunate reality in application,” the Texas Supreme Court in \textit{TXU} appears to have fallen into the familiar trap of talking out of both sides of its mouth when it comes to the reasonableness of liquidated damages.\(^{234}\) While its decision did little to alleviate the confusing language courts have used in dealing with this issue, one thing it appears the court did resolve is that Texas follows the second-look approach to the reasonableness analysis.\(^{235}\) This is likely to be better news for defendants than for plaintiffs because it gives defendants an “ace in the hole” of avoiding onerous liquidated damages provisions by proving that actual damages were less than the amount stipulated in the contract.

The adoption of the UCC in Texas for contracts involving the sale of goods further convoluted what was already a confusing issue.\(^{236}\) While the court’s decision in \textit{TXU} did not specifically address contracts under the UCC, it seems likely that a similar retrospective approach, in which more emphasis is placed on actual damages than what the parties may have decided amongst themselves was reasonable at the moment of contracting, would be applied in that context as well.

Though there are certainly cases that would appear to point to the contrary, this may have been the Texas position as far back as \textit{Collier v. Betterton} in 1895.\(^{237}\) Whatever the case, it seems to be the Texas position now.\(^{238}\) Thus, practitioners should always be cognizant of the fact that any liquidated damages clause, however reasonable it may seem at the outset, will be subject to a second-look in light of the actual damages sustained. Though this approach may detract from the confidence parties have that courts will enforce their mutual bargains, it helps assure that illegal

\(^{233}\) \textit{Wassenaar v. Panos,} 331 N.W.2d 357, 363 (Wis. 1983).

\(^{234}\) \textit{TXU,} 426 S.W.3d at 70–72.

\(^{235}\) \textit{See id. at} 72.

\(^{236}\) \textit{Anderson, supra} note 8, at 1091.

\(^{237}\) 29 S.W. 467, 468 (Tex. 1895).

\(^{238}\) \textit{See generally TXU,} 426 S.W.3d at 72.
penalties cannot be dressed up as liquidated damages clauses. The most practitioners can do now in drafting a liquidated damages clause is try to make it appear as reasonable as possible at the time of contracting. But as to whether it will actually be enforced or not, as one blogger recently wrote in response to the *TXU* case, you may need to “get out your crystal ball.”\(^{239}\)