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Home and business owners increasingly rely on alarm systems to protect against theft and property damage. When a burglary or fire occurs and an alarm service customer discovers that the alarm company negligently failed to call the police or fire department, the customer understandably would expect redress for the company's failure to provide its service. Many customers would be surprised, though, to discover that an alarm company's liability is often contractually limited to a relatively token amount unrelated to the cost of the service, even when the alarm company is negligent.

Some states view these limitations of liability as exculpatory clauses and determine their enforceability based on whether they are unconscionable or violate public policy. Other states view them as liquidated damages and apply a penalty test to determine their enforceability. This Note addresses the differences between these two approaches in the context of the unique remedy difficulties inherent in alarm service contracts. This Note then argues that the prevailing policy rationales for enforcing alarm service provisions that limit a party's liability for its own negligence are misguided and advocates that these provisions should not be enforced as a matter of public policy.

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INTRODUCTION

After a long day of work, the manager of a grocery store ends his evening shift, as he always does, by setting the store's burglar alarm and locking the building. Just as he is about to get in his car and head home for the day, however, an armed robber accosts him in the parking lot and forces him to return to the store at gunpoint. Against his will, the manager leads the robber into the grocery's inner office and opens the store's safe. The robber then ties up the manager with tape and proceeds to empty the safe. Throughout this terrifying ordeal, the manager's only comfort was that he did not disarm the burglar alarm when he unlocked the store. Surely the police would arrive soon.

Despite receiving the alarm signal, the burglar alarm company does not notify the police, and the robber makes his getaway fourteen minutes after the alarm first activates. It is not until after the robber flees with over $35,000 from the safe that the manager, still bound with tape, is able to maneuver to a telephone and call for help. The police arrive two minutes later—too late to catch the robber.

This scenario is based on the facts of *Better Food Markets v. American District Telephone Co.*,[1] where the California Supreme Court ruled there was sufficient evidence for a jury to reasonably find that the alarm company's failure to perform its contractual duty to notify the police was the proximate cause of the grocery store's $35,930 loss.[2] Nevertheless, the

1. 253 P.2d 10 (Cal. 1953).
2. *Id.* at 12–13.

court limited the grocery store's recovery to $50.[3] Why only $50? Because the burglar alarm contract provided that "liability . . . shall be limited to and fixed at the sum of fifty dollars as liquidated damages, and not as a penalty, and this liability shall be exclusive."[4]

Many home and business monitoring service contracts contain similar provisions[5] and customers, who are often surprised to find that these provisions apply even when the alarm company is at fault, have a strong incentive to challenge the enforceability of these clauses.[6] Different states apply different tests to determine the enforceability of contract clauses that, like the provision in *Better Food Markets*, limit a party's liability to a specific dollar amount for damages caused by negligence.[7]

Scholars have observed the distinction between liquidated damages and limitation-of-liability clauses,[8] discussed the enforceability of exculpatory[9] and liquidated damages[10] clauses in general, and examined the enforceability of limitation-of-liability clauses in specific areas such as professional service contracts.[11] However, none have addressed the unique policy concerns generated by limitation-of-liability clauses in alarm service contracts. This Note discusses the inconsistent manner in which states determine the enforceability of such provisions and analyzes whether these provisions should be enforced. Some jurisdictions, such as Connecticut,

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3. *Id.* at 16.

4. *Id.* at 13.

5. *See generally* Marjorie A. Shields, Annotation, *Validity, Construction, and Application of Exculpatory and Limitation of Liability Clauses in Burglary, Fire, and Other Home and Business Monitoring Service Contracts*, 36 A.L.R.6th 305 (2008).

6. *See* Eric Dexheimer, *With Failures, Alarm Companies Have Little Liability*, MYSTATESMAN (Jan. 25, 2014, 7:48 PM), http://www.mystatesman.com/news/news/with-failures-alarm-companies-have-little-liabilit/nc3Dj/ [https://perma.cc/6WAP-DTQY]. As alarm systems grow more sophisticated, these lawsuits may become more common. *See* Complaint at 1, Hernandez v. ADT Corp., No. 9:16-cv-80335 (S.D. Fla. Mar. 7, 2016) (alleging that ADT's wireless signals can be "intercepted and interfered with by unauthorized third parties"); *see also* Emily Field, *Suit Says ADT Security Systems Leave Homes Vulnerable*, LAW360 (Mar. 8, 2016, 4:51 PM), http://www.law360.com/articles/768812 [https://perma.cc/XT9T-7LCY]; Kashmir Hill, *How Your Security System Could Be Hacked to Spy on You*, FORBES (July 23, 2014, 6:30 AM), http://www.forbes.com/sites/kashmirhill/2014/07/23/how-your-security-system-could-be-used-to-spy-on-you/#3bf21146198b [https://perma.cc/2X9X-RDRB].

7. *See infra* Part II.

8. *See generally* William F. Fritz, *"Underliquidated" Damages as Limitation of Liability*, 33 TEX. L. REV. 196 (1954); Debora L. Threedy, *Liquidated and Limited Damages and the Revision of Article 2: An Opportunity to Rethink the U.C.C.'s Treatment of Agreed Remedies*, 27 IDAHO L. REV. 427 (1991); Elizabeth Warren, *Formal and Operative Rules Under Common Law and Code*, 30 UCLA L. REV. 898 (1983).

9. *See generally* Scott J. Burnham, *Are You Free to Contract Away Your Right to Bring a Negligence Claim?*, 89 CHI.-KENT L. REV. 379 (2014); Lynn Guissinger, Note, *Exculpatory Clauses and Public Policy: A Judicial Dilemma*, 53 U. COLO. L. REV. 793 (1982).

10. *See generally* Charles J. Goetz & Robert E. Scott, *Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach*, 77 COLUM. L. REV. 554 (1977).

11. *See generally* John Terwilleger, Note, *Can a Professional Limit Liability Contractually Under Florida Law?*, 65 FLA. L. REV. 1351 (2013).

have yet to definitively weigh in on which test they will use,[12] providing them with an opportunity to choose the best method of determining the enforceability of these limitation-of-liability provisions.

Part I of this Note provides an overview of three types of contractual provisions that manage liability: exculpatory clauses, liquidated damages clauses, and limitation-of-liability clauses. Part II explores the two primary tests that states use to determine the enforceability of limitation-of-liability clauses like the clause in *Better Food Markets*. Finally, Part III considers the better test to determine the enforceability of limitation-of-liability clauses that limit a party's liability to a specific dollar amount for damages caused by negligence. It then argues that such clauses should not be enforceable in alarm service contracts—courts should find them unconscionable, and legislatures should declare them void as a matter public policy.

I. EXCULPATORY, LIQUIDATED DAMAGES, AND LIMITATION-OF-LIABILITY CLAUSES: THREE METHODS TO MANAGE LIABILITY

Contracts often contain provisions designed to limit the scope of a party's liability. Exculpatory clauses are designed to relieve a party from liability for a negligent or wrongful act.[13] Liquidated damages clauses determine, in advance, the measure of damages if a party breaches a contract.[14] A hybrid of these two types of contractual clauses, limitation-of-liability clauses, restrict the measure of damages regardless of the actual damages ultimately suffered.[15] Unlike liquidated damages clauses, limitation-of-liability clauses do not purport to estimate the harm caused by a breach.[16] In contrast to exculpatory clauses, however, limitation-of-liability clauses do not completely disclaim liability for a party's negligence; rather, such clauses limit recoverable damages beyond a specific (maximum) dollar amount.[17]

Part I.A discusses exculpatory clauses and the traditional methods of determining their enforceability: addressing whether a contract is procedurally and substantively unconscionable or whether the clause violates public policy. Part I.B discusses liquidated damages clauses, distinguishes between overliquidated and underliquidated damages, and details the traditional tests to determine their enforceability. Finally, Part

12. *See infra* Part II.C.
13. *See Exculpatory Clause*, BLACK'S LAW DICTIONARY (10th ed. 2014).
14. *Liquidated Damages Clause*, BLACK'S LAW DICTIONARY (10th ed. 2014).
15. *See* Nahra v. Honeywell, Inc., 892 F. Supp. 962, 969 (N.D. Ohio 1995).
16. *See* RESTATEMENT (FIRST) OF CONTRACTS § 339 cmt. g (AM. LAW INST. 1932).
17. *See* Wedner v. Fid. Sec. Sys., Inc., 307 A.2d 429, 431 (Pa. Super. Ct. 1973) (describing a limitation-of-liability clause as allowing recovery up to a contracted amount, beyond which further recovery is unavailable); Terwilleger, *supra* note 11, at 1365 ("[T]here is a key difference between exculpatory clauses and limitation of liability clauses, because an exculpatory clause 'insulates a party from liability,' while a limitation of liability clause 'merely places a limit upon that liability.'" (quoting Valhal Corp. v. Sullivan Assocs., Inc., 44 F.3d 195, 202 (3d Cir. 1995))).

I.C describes limitation-of-liability clauses in alarm service contracts—the primary focus of this Note—and addresses whether they should be characterized as exculpatory clauses or liquidated damages clauses for enforceability purposes.

A. Exculpatory Clauses, Unconscionability, and Public Policy

To determine the enforceability of an exculpatory clause that denies an injured party the right to recover damages from another's negligence, courts typically analyze whether the clause is unconscionable or void as a matter of public policy.[18] Part I.A.1 and I.A.2 provide an overview of unconscionability doctrine and public policy considerations, respectively.

1. Unconscionability Doctrine

Unconscionability refers to the "absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party."[19] Traditionally, a contract was said to be unconscionable if it was "such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other."[20] Today, a showing of unconscionability generally requires two elements: procedural unconscionability and substantive unconscionability.[21]

Procedural unconscionability refers to "whether the imposed-upon party had meaningful choice about whether and how to enter into the transaction."[22] By itself, an unequal bargaining position between parties does not make a contract procedurally unconscionable.[23] However, gross inequality of bargaining power weighs in favor of finding that the weaker party had no meaningful choice in assenting to the contract's terms, especially in the presence of factors such as

> belief by the stronger party that there is no reasonable probability that the weaker party will fully perform the contract; knowledge of the stronger party that the weaker party will be unable to receive substantial benefits from the contract; [and] knowledge of the stronger party that the weaker

18. *See* 17A AM. JUR. 2D *Contracts* § 283 (2004).

19. Williams v. Walker-Thomas Furniture Co., 350 F.2d 445, 449 (D.C. Cir. 1965); *accord* Desiderio v. Nat'l Ass'n of Sec. Dealers, 191 F.3d 198, 207 (2d Cir. 1999).

20. RESTATEMENT (SECOND) OF CONTRACTS § 208 cmt. b (AM. LAW INST. 1981) (quoting Hume v. United States, 132 U.S. 406, 411 (1889)).

21. *See* 8 SAMUEL WILLISTON & RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS § 18:10 (4th ed. 2010); *see also* Burnham, *supra* note 9, at 381 ("In the classical construct both [procedural and substantive unconscionability] are necessary for a finding of unconscionability.").

22. 8 WILLISTON & LORD, *supra* note 21, § 18:10. Indeed, one of the fundamental rationales for setting aside contracts as unconscionable is to protect "parties with weak bargaining power from contractual overreaching by those with stronger bargaining power." Stephen Friedman, *Arbitration Provisions: Little Darlings and Little Monsters*, 79 FORDHAM L. REV. 2035, 2043 (2011).

23. RESTATEMENT (SECOND) OF CONTRACTS § 208 cmt. d.

> party is unable reasonably to protect his interests by reason of physical or mental infirmities, ignorance, illiteracy or inability to understand the language of the agreement, or similar factors.[24]

For example, a contract may be procedurally unconscionable where the nondrafting party with an obvious lack of education did not have a reasonable opportunity to understand the contract's terms because the terms were "hidden in a maze of fine print and minimized by deceptive sales practices."[25]

Often, exculpatory clauses are found in standard-form contracts that are offered on a "take it or leave it" basis, known as contracts of adhesion.[26] However, the mere fact that an exculpatory clause appears in an adhesion contract is not enough to establish procedural unconscionability.[27] Instead, "[t]here must be an additional showing of great disparity in bargaining power between the parties, of lack of opportunity for negotiation, or of inability to obtain the offered services elsewhere."[28] In contracts between large businesses and consumers, the ability of the consumer to obtain the services elsewhere is often the dispositive factor in determining procedural unconscionability.[29] As long as the consumer is free to "leave it"—forgo the service or obtain it elsewhere—even an adhesion contract is unlikely to be procedurally unconscionable.[30] Accordingly, the existence of a market for the service weighs against a finding of procedural unconscionability.[31] This is consistent with economists' views that exculpatory clauses, like other contract terms, are "matter[s] of individual liberty that should be left to the market."[32]

Substantive unconscionability refers to whether the terms of a contract are unreasonably favorable to the stronger party.[33] Factors that favor a finding of substantive unconscionability include terms that contravene public interest or public policy, terms that impermissibly alter fundamental duties imposed by law, provisions that negate the reasonable expectations of the nondrafting party, and terms that are unreasonably and unexpectedly harsh that benefit the drafting party at the nondrafting party's expense.[34] When determining substantive unconscionability, courts look for "terms that are so oppressive that no reasonable person would make them and no fair and honest person would accept them."[35] Notably, courts will not

24. *Id.*
25. Williams v. Walker-Thomas Furniture Co., 350 F.2d 445, 449 (D.C. Cir. 1965).
26. *See* Burnham, *supra* note 9, at 381; Guissinger, *supra* note 9, at 795.
27. *See* Burnham, *supra* note 9, at 381.
28. Guissinger, *supra* note 9, at 795.
29. *See id.* at 798.
30. *See id.* at 799–800.
31. Burnham, *supra* note 9, at 383.
32. *Id.* at 380.
33. *See* 8 WILLISTON & LORD, *supra* note 21, § 18:10.
34. *Id.*
35. Burnham, *supra* note 9, at 384.

enforce exculpatory clauses that attempt to insulate a tortfeasor from gross—willful or wanton—negligence.[36]

To determine the overall enforceability of a provision, courts often balance procedural and substantive unconscionability.[37] In this manner, "the greater the harshness or unreasonableness of the substantive terms, the less important the regularity of the process of contract formation that gave rise to the term becomes."[38] Likewise, "[w]hen there is clear procedural unconscionability, . . . even minimal substantive unfairness may be enough to justify declaring the contract or clause unconscionable, and even a substantively fair bargain may be declared unconscionable if the procedural defects are great enough."[39]

2. Public Policy

Closely related to the notion that a court should not enforce an unconscionable contract is the doctrine that a court should not enforce a contract that violates public policy. A finding that a provision violates public policy is based on the idea that "an obligation of care owed by one person to another outweigh[s] [the] traditional regard for freedom of contract."[40] While public policy determinations depend on the circumstances of each case,[41] the Supreme Court of California articulated six commonly cited factors[42] in *Tunkl v. Regents of University of California*[43] typical of exculpatory clauses that are invalid as against public policy: (1) the business is "generally thought suitable for public regulation"; (2) the service is of great importance to the public and "often a matter of practical necessity for some members of the public"; (3) the service provider holds itself out as willing to provide it to any member of the public (who meets certain established standards); (4) because of the essential nature of the service, the provider has a decisive advantage in bargaining power; (5) the provider employs standardized contracts and makes no provision for purchasers to pay an additional (reasonable) fee to protect against negligence; and (6) "as a result of the transaction, the person or property of the purchaser is placed under the control of the seller, subject to the risk of carelessness by the seller or his agents."[44]

In summary, a court may refuse to enforce an exculpatory clause that denies an injured party the right to recover damages from another's negligence if the court finds that the clause is unconscionable or contrary to public policy. After such a finding, a court may (1) refuse to enforce the

36. *See* Fritz, *supra* note 8, at 209; Guissinger, *supra* note 9, at 795 n.6 (citing Jones v. Dressel, 623 P.2d 370, 376 (Colo. 1981)).

37. *See* 8 WILLISTON & LORD, *supra* note 21, § 18:14.

38. *Id.*

39. *Id.*

40. Scott v. Pac. W. Mountain Resort, 834 P.2d 6, 11 (Wash. 1992).

41. *See* 17A AM. JUR. 2D *Contracts* § 283 (2004).

42. *See* Dalury v. S-K-I, Ltd., 670 A.2d 795, 798 (Vt. 1995) ("Numerous courts have adopted and applied the *Tunkl* factors.").

43. 383 P.2d 441 (Cal. 1963).

44. *Id.* at 444–46 (footnotes omitted).

contract, (2) enforce the remainder of the contract without the exculpatory clause, or (3) limit the application of the exculpatory clause to avoid the undesirable result.[45] In the context of a negligence action, finding an exculpatory clause to be unconscionable or contrary to public policy would mean that the plaintiff would not be contractually barred from pursuing her underlying claim.

B. Liquidated Damages Clauses and the Penalty Test

Liquidated damages clauses, which specify an agreed amount of damages for a breach of contract, are subject to strict judicial scrutiny.[46] In contrast to exculpatory clauses, the validity of a liquidated damages clause depends on (1) whether the specified amount is a reasonable estimate of anticipated or actual damages from a breach and (2) whether such damages would be difficult to prove.[47] A provision that fails to satisfy both criteria is deemed an unenforceable penalty,[48] which is why this is known as the "penalty rule" or the "penalty test."

The two prongs of this test are closely related in that the reasonableness of the fixed damages is proportional to the difficulty of proving actual loss or establishing the amount of actual loss with certainty.[49] "If the difficulty of proof of loss is great, considerable latitude is allowed in the approximation of anticipated or actual harm. If, on the other hand, the difficulty of proof of loss is slight, less latitude is allowed in that approximation."[50]

While parties are free to fix reasonable damages by contract when actual damages would be difficult to estimate or prove, parties are not free to provide penalties for breach.[51] This is because contract remedies are intended to be compensatory, not punitive.[52] A liquidated damages clause violates public policy and is termed a "penalty" when it has the intended or actual effect of punishing a party for breaching a contract.[53] Essentially, a liquidated damages clause must not create such a large disparity between the negotiated damages and the actual damages likely to be caused by a breach that it acts *in terrorem* to induce performance by making a breach

45. *See* RESTATEMENT (SECOND) OF CONTRACTS § 208 (AM. LAW INST. 1981).

46. *See* Goetz & Scott, *supra* note 10, at 554 ("For more than five centuries, strict judicial scrutiny has been applied to contractual provisions which specify an agreed amount of damages upon breach of a base obligation.").

47. *See* RESTATEMENT (SECOND) OF CONTRACTS § 356.

48. *See* 24 SAMUEL WILLISTON & RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS § 65:1 (4th ed. 2002).

49. *See* RESTATEMENT (SECOND) OF CONTRACTS § 356 cmt. b.

50. *Id.*

51. *See id.* § 356 cmt. a.

52. *Id.*; *see* Fritz, *supra* note 8, at 197–98 ("[A] court will enforce an agreement for the payment of a stipulated sum, whether it is denominated liquidated damages or penalty, only where the court finds that the parties in fact intended its payment *as compensation for the anticipated breach, having due regard for the principles of compensation as worked out by the courts*.").

53. *See* 24 WILLISTON & LORD, *supra* note 48, § 65:1.

unreasonably costly.[54] Once designated a penalty, a clause that attempts to liquidate damages "will not be enforced despite the expressed intention of the parties."[55] In theory, the penalty rule protects against both the unfair recovery by the nonbreaching party in the event of breach, as well as the inefficient performance of a contract by the other party when it would otherwise be economically efficient to breach.[56]

Liquidated damages clauses can be overcompensatory or undercompensatory.[57] The typical liquidated damages case involves overcompensatory damages, which are damages greater than those traditionally available under contract law.[58] In such a case, "it is the breaching party who attacks the enforceability of the liquidated damages clause."[59] However, in an undercompensatory liquidated damages case, the damages an aggrieved party can prove under traditional contract law exceed the liquidated damages.[60] In contrast to the typical case, then, these "underliquidated" damages become "the breaching party's shield from provable damages rather than the aggrieved party's sword for enhanced damages. The judge must decide if the underliquidated damages clause is the exclusive remedy or if the plaintiff may instead recover actual damages or specific performance."[61]

If enforced, an underliquidated damages clause denies the aggrieved party its traditional contract remedies and functions effectively as a limitation-of-liability clause.[62] If, however, a court rules that an underliquidated damages clause is unenforceable, the plaintiff is no longer contractually prohibited from proving and collecting actual damages.[63]

C. Limitation-of-Liability Clauses

If unconscionability doctrine and public policy determine the enforceability of exculpatory clauses, and the penalty test determines the enforceability of liquidated damages clauses, then what is the proper test to determine the enforceability of limitation-of-liability clauses? To help answer this question, Part I.C.1 provides a general overview of limitation-of-liability clauses. Then, Part I.C.2 describes the particular limitation-of-liability provisions characteristic of alarm service contracts.

54. *Id.*
55. Goetz & Scott, *supra* note 10, at 576.
56. *See id.* at 556.
57. *See* Threedy, *supra* note 8, at 429.
58. Warren, *supra* note 8, at 901.
59. Threedy, *supra* note 8, at 429.
60. *See* Warren, *supra* note 8, at 901.
61. *Id.*
62. *Id.* at 902 n.21.
63. *See id.* at 906.

1. Limitations of Liability

Generally, limitation-of-liability clauses are scrutinized under the same unconscionability or public policy standards as exculpatory clauses.[64] This tends to be true even where, as in the *Better Food Markets* contract, the clause is described as a liquidated damages provision.[65]

One rationale for applying the test for exculpatory clauses rather than the test for liquidated damages clauses is that, unlike a penalty, a limitation-of-liability clause does not operate *in terrorem* to induce performance by making a breach unreasonably costly.[66] "[T]o apply literally the concept of 'penalty' to test performance of underliquidated damages is patent nonsense. No underliquidated damages clause will ever penalize the breaching party."[67]

Another rationale for distinguishing limitation-of-liability clauses from liquidated damages clauses stems from their different evidentiary burdens at trial. "[T]he purpose of a liquidated damages provision is to obviate the need for the nonbreaching party to prove actual damages."[68] After establishing proof of breach, the aggrieved party is entitled to the liquidated amount without having to establish the exact amount of actual damages.[69] Where a limitation of liability is present, though, a plaintiff is required to prove actual damages as part of her claim.[70] In this manner, a limitation of liability represents a damages ceiling rather than a stipulation of damages.

Furthermore, limitation-of-liability clauses and overcompensatory liquidated damages may present differing fairness concerns. In some sense, both might seem "as repugnant" because they both "deny to the promisee the remedy for nonperformance which the law normally affords him."[71] However, overcompensatory liquidated damages provide an unjustified gain to a party, while limitation-of-liability clauses burden a party with an uncompensated loss.[72] The latter instance might be justified as merely an unsavory consequence of a party's right to contract away its remedies (as with exculpatory clauses), but there are no "comparable rights lying on the stricter side of contract" to justify the former, which attempts to exercise more power than traditionally allowed under contract law.[73]

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64. *See* 24 WILLISTON & LORD, *supra* note 48, § 65:6.
65. *See id. But see infra* Part II.B.
66. *See* 24 WILLISTON & LORD, *supra* note 48, § 65:6.
67. Warren, *supra* note 8, at 906 n.46.
68. Bair v. Axiom Design, L.L.C., 2001 UT 20, ¶ 25, 20 P.3d 388, 394.
69. *See* 24 WILLISTON & LORD, *supra* note 48, § 65:33.
70. *See* Mary G. Leary, *Liability for Security or Burglar Alarm System Failure*, 72 AM. JUR. PROOF OF FACTS 3D 1, 64 (2003); *see also* Fritz, *supra* note 8, at 201 n.17 ("A valid liquidated damages agreement permits recovery without proof of actual loss . . . . An agreement for limitation of liability does not in terms promise the payment of any sum; actual damages must be proved in the usual fashion to the amount recoverable within the limit fixed.").
71. Fritz, *supra* note 8, at 220.
72. *See id.*
73. Ian R. Macneil, *Power of Contract and Agreed Remedies*, 47 CORNELL L.Q. 495, 511 n.54 (1962); *accord* Threedy, *supra* note 8, at 430 n.13 ("The rationale for this

2. Limitations of Liability in Alarm Service Contracts

Alarm service contracts commonly contain a limitation-of-liability clause.[74] The contested provision in *Nahra v. Honeywell, Inc.*,[75] provides an illustrative example:

> It is understood and agreed by the parties hereto that Honeywell is providing a system designed to reduce the risk of loss; that the payments provided herein are based solely on the value of the services as described herein and are unrelated to the value of any property located on Customer's premises; that Honeywell is not liable for losses which may occur in cases of malfunction or nonfunction of the system or of the monitoring, repairing, signaling [sic] handling or dispatching of the service, even if due to Honeywell's negligence or failure of performance; that Honeywell is not an insurer; and that insurance, if any, covering personal injury and/or property loss or damage on customer's premises shall be obtained and or maintained by Customer. Customer understands that Honeywell offers several levels of protection and services and that the system described in the Schedule of Service and Protection has been chosen by Customer after considering and balancing the levels of protection afforded by various systems and the related costs.
>
> IT IS AGREED THAT IT IS IMPRACTICAL AND EXTREMELY DIFFICULT TO FIX ACTUAL DAMAGES WHICH MAY ARISE IN SITUATIONS WHERE THERE MAY BE A FAILURE OF SERVICES PROVIDED, DUE TO THE UNCERTAIN VALUE OF CUSTOMER'S PROPERTY OR THE PROPERTY OF OTHERS KEPT ON THE PROTECTED PREMISES WHICH MAY BE LOST, STOLEN, DESTROYED, DAMAGED OR OTHERWISE AFFECTED BY OCCURRENCES WHICH THE SYSTEM OR SERVICE IS DESIGNED TO DETECT OR AVERT. INABILITY OF CONTRACTOR TO GUARANTEE POLICE AND FIRE DEPARTMENT RESPONSE TIME, AND ESTABLISHING A CASUAL [SIC] CONNECTION BETWEEN THE SYSTEM OR SERVICE PROBLEMS AND CUSTOMER'S POSSIBLE LOSS. THEREFORE IF ANY LIABILITY IS IMPOSED ON HONEYWELL, SUCH LIABILITY SHALL BE LIMITED TO AN AMOUNT EQUAL TO THE ANNUAL SERVICE CHARGE OR $10,000, WHICHEVER IS LESS. (IF THERE IS NO ANNUAL SERVICE CHARGE, HONEYWELL'S LIABILITY SHALL BE LIMITED TO $500.00.) [SIC] THIS SUM SHALL BE PAID AND RECEIVED EITHER (i) AS LIQUIDATED DAMAGES AND NOT AS A PENALTY, OR (ii) AS A LIMITATION OF LIABILITY APPROVED AND AGREED UPON BY THE PARTIES. THE PAYMENT OF THIS AMOUNT SHALL BE HONEYWELL'S SOLE AND EXCLUSIVE LIABILITY REGARDLESS OF WHETHER LOSS OR DAMAGE IS CAUSED BY THE PERFORMANCE OR NONPERFORMANCE OF OBLIGATIONS UNDER THIS CONTRACT OR BY NEGLIGENCE, ACTIVE OR OTHERWISE, OF HONEYWELL, ITS EMPLOYEES,

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difference is that a party may waive or give up a right but may not contract for more than is allowable.").

74. *See supra* note 5 and accompanying text.

75. 892 F. Supp. 962 (N.D. Ohio 1995).

> AGENTS OR REPRESENTATIVES. NO SUIT OR ACTION SHALL BE BROUGHT AGAINST HONEYWELL MORE THAN ONE (1) YEAR AFTER THE ACCRUAL OF THE CAUSE OF ACTION THEREFOR.[76]

A few things from this excerpt are worth noting because they are characteristic of alarm service contracts and central to litigation challenging their enforceability: (1) it contains a provision that disclaims the alarm company's liability for losses caused by its own negligence and failure of performance, (2) it notes that the alarm company "is not an insurer," (3) it states that actual damages are impractical and extremely difficult to fix, and (4) it provides for a fixed limit to the alarm company's liability "as liquidated damages and not as a penalty" *or* "as a limitation of liability."[77]

One aspect of the *Nahra* contract that varies from case to case is the amount of damages specified as a limit. In *Nahra*, this amount is the lesser of the annual service charge or $10,000 (or $500 in the absence of an annual service charge).[78] The lesser of the two amounts in *Nahra* was the annual service charge, which totaled $2,124.[79] In contrast, the amount specified in the *Better Food Markets* contract was $50, an amount unrelated to the cost of the service.[80] While the amount varies between contracts, alarm service limitation-of-liability clauses typically provide for damages in one of four ways: (1) a specific dollar amount;[81] (2) the cost of service or a specific dollar amount, whichever is lesser;[82] (3) the cost of service or a specific dollar amount, whichever is greater;[83] or (4) the cost of service.[84]

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76. *Id.* at 964–65 (alterations in original).

77. *See id.*

78. *Id.*

79. *See id.* at 964 ("Plaintiffs agreed to pay a $177 monthly service fee.").

80. *See* Better Food Mkts. v. Am. Dist. Tel. Co., 253 P.2d 10, 13 (Cal. 1953).

81. *See* Donegal Mut. Ins. v. Tri-Plex Sec. Alarm Sys., 622 A.2d 1086, 1088 (Del. Super. Ct. 1992) ($250); Bargaintown of D.C., Inc. v. Fed. Eng'g Co. of Wash., D.C., 309 A.2d 56, 56–57 (D.C. 1973) ($25); Samson Sales, Inc. v. Honeywell, Inc., 465 N.E.2d 392, 393 (Ohio 1984) ($50); Arthur's Garage, Inc. v. Racal-Chubb Sec. Sys., Inc., 997 S.W.2d 803, 809 (Tex. App. 1999) ($350).

82. *See* Gen. Bargain Ctr. v. Am. Alarm Co., 430 N.E.2d 407, 408 (Ind. Ct. App. 1982) ("$250, or an amount equal to six monthly payments of $46.30 each, whichever [is] the lesser."); Schrier v. Beltway Alarm Co., 533 A.2d 1316, 1318 (Md. Ct. Spec. App. 1987) (providing for six monthly payments of $49.50 per month or $250.00, "whichever is the lesser"); Morgan Co. v. Minn. Mining & Mfg. Co., 246 N.W.2d 443, 447 (Minn. 1976) ("[S]ix (6) times the total monthly charge shown herein [of $82 per month], or . . . [$250.00], whichever sum shall be less."); Sanif, Inc. v. Iannotti, 500 N.Y.S.2d 798, 799 (App. Div. 1986) (providing for 10 percent of the $180 installation price or $250.00, "whichever is lesser").

83. *See* Braden v. Honeywell, Inc., 8 F. Supp. 2d 724, 726 (S.D. Ohio 1998) ("[S]ix (6) times the [$150] monthly charge . . . or $250 whichever is greater."); Tessler & Son, Inc. v. Sonitrol Sec. Sys. of N. N.J., Inc., 497 A.2d 530, 532 (N.J. Super. Ct. App. Div. 1985) ("[T]en percent of the [$600] annual monitoring charge for the premises or $250 whichever is greater.").

84. *See* Cent. Alarm of Tucson v. Ganem, 567 P.2d 1203, 1206 (Ariz. Ct. App. 1977) ("[A] sum equal in amount to the [$43 per month] rental service charged hereunder for a period of service not to exceed six months."); Wedner v. Fid. Sec. Sys., Inc., 307 A.2d 429, 430–31 (Pa. Super. Ct. 1973) ("[T]he yearly service charge [of $312].").

One explanation for the peculiarity of the damages specified by these provisions may lie in the ongoing nature of alarm service contracts. In contrast to service contracts that are one-shot deals, contracts that provide a full refund in the event that an alarm service company fails to provide its service, which would at least protect a customer's restitution interest,[85] may leave a customer better off than her precontract position. For example, assume that a store equipped with an alarm experienced five burglaries in one year. If the alarm service company negligently failed to call the police during only one of those burglaries but must nevertheless pay restitution for the cost of the full year's service, then the store will have benefitted—free of charge—from the alarm company's protection during the four other burglaries.

As with exculpatory clauses[86] and liquidated damages clauses,[87] if a court finds a limitation-of-liability clause unenforceable, the plaintiff is no longer contractually prohibited from seeking actual damages for her underlying claim.[88] When an alarm company negligently fails to provide its service, plaintiffs often allege both negligence and breach of contract simultaneously.[89]

II. DIFFERENT APPROACHES TO DETERMINE THE ENFORCEABILITY OF LIMITATION-OF-LIABILITY CLAUSES

There is a certain "schizophrenic quality of the law" when it comes to determining the enforceability of underliquidated damages clauses,[90] and this is no less true when it comes to the enforceability of limitation-of-liability clauses in alarm service contracts. Most states determine the enforceability of limitation-of-liability clauses in home and business monitoring service contracts by using the same unconscionability and public policy analysis used for exculpatory clauses, but some state courts analyze these provisions as they would liquidated damages clauses. Meanwhile, some courts have yet to take a definitive stance regarding whether they will follow the majority or minority rule.

Part II.A addresses the approach taken by a majority of courts, which analyzes limitation-of-liability clauses as exculpatory clauses for enforceability purposes. Next, Part II.B describes the minority approach of applying the penalty test to determine the enforceability of limitation-of-

85. *See Restitution*, BLACK'S LAW DICTIONARY (10th ed. 2014) (describing restitution as a remedy "in which the measure of recovery is usu[ally] based not on the plaintiff's loss, but on the defendant's gain").

86. *See supra* note 45 and accompanying text.

87. *See supra* note 63 and accompanying text.

88. *See* Wyer v. Sonitrol Sec. Sys. of Hartford, Inc., 738 A.2d 1179, 1183 (Conn. Super. Ct. 1999) (finding a limitation-of-liability clause unenforceable, thereby allowing the plaintiffs to proceed past summary judgment with their claim).

89. *See id.* at 1180 ("This action has been brought in two counts. Count one is in negligence, and count two is in breach of contract."); *see also* Braden v. Honeywell, Inc., 8 F. Supp. 2d 724, 724 (S.D. Ohio 1998) ("Plaintiffs . . . bring this diversity action asserting claims of breach of contract and negligence against defendant Honeywell, Inc.").

90. Threedy, *supra* note 8, at 453.

liability clauses. Then, Part II.C discusses several jurisdictions where the rule is uncertain, either because courts apply both tests or because state supreme or appellate-level courts have yet to issue a definitive ruling. In particular, this section discusses the uncertainty in Connecticut, where state appellate-level courts have not issued a decision interpreting the validity of limitation-of-liability provisions in alarm service contracts.[91]

A. The Majority Rule: Limitation-of-Liability Clauses Are Enforceable Unless Unconscionable or Against Public Policy

Of the states that have addressed the issue, a majority determine the enforceability of limitation-of-liability clauses that place a cap on recoverable damages from one party's negligence by analyzing whether such clauses are unconscionable or void as a matter of public policy.[92] For example, in *Morgan Co. v. Minnesota Mining & Manufacturing Co.*,[93] the Supreme Court of Minnesota upheld a provision in a burglar alarm system contract that limited an alarm seller's liability for losses caused by the negligence of its employees to $250 because the provision was not unconscionable nor did it violate public policy.[94] There, the Minnesota court refused to analyze the provision as it would a liquidated damages clause despite the use of the words "liquidated damages" in the contract.[95]

The Restatement (Second) of Contracts distinguishes limitation-of-liability clauses like the clause in *Morgan* from traditional liquidated damages clauses because the former attempt to fix unreasonably small,

91. *See* Forster v. Advanced Elec. Servs., Inc., No. X03CV010510854S, 2002 WL 31463511, at *3 (Conn. Super. Ct. Oct. 15, 2002).

92. *See* Fox Alarm Co. v. Wadsworth, 913 So. 2d 1070 (Ala. 2005); Cent. Alarm of Tucson v. Ganem, 567 P.2d 1203 (Ariz. Ct. App. 1977); Nat'l Union Fire Ins. of Pittsburgh v. Guardtronic, Inc., 64 S.W.3d 779 (Ark. Ct. App. 2002); Donegal Mut. Ins. v. Tri-Plex Sec. Alarm Sys., 622 A.2d 1086 (Del. Super. Ct. 1992); L. Luria & Son, Inc. *ex rel.* Fireman's Fund Ins. v. Alarmtec Int'l Corp., 384 So. 2d 947 (Fla. Dist. Ct. App. 1980); Steiner Corp. v. Am. Dist. Tel., 683 P.2d 435 (Idaho 1984); Purolator Sec., Inc. v. Wells Fargo Alarm Serv., 491 N.E.2d 161 (Ill. App. Ct. 1986); Corral v. Rollins Protective Servs. Co., 732 P.2d 1260 (Kan. 1987); United Servs. Auto. Ass'n v. ADT Sec. Servs., Inc., 241 S.W.3d 335 (Ky. Ct. App. 2006); Lazybug Shops, Inc. v. Am. Dist. Tel. Co., 374 So. 2d 183 (La. Ct. App. 1979); St. Paul Fire & Marine Ins. v. Guardian Alarm Co. of Mich., 320 N.W.2d 244 (Mich. Ct. App. 1982); Morgan Co. v. Minn. Mining & Mfg. Co., 246 N.W.2d 443 (Minn. 1976); Purcell Tire & Rubber Co. v. Exec. Beechcraft, Inc., 59 S.W.3d 505 (Mo. 2001); New Light Co. v. Wells Fargo Alarm Servs., 525 N.W.2d 25 (Neb. 1994); Tessler & Son, Inc. v. Sonitrol Sec. Sys. of N. N.J., Inc., 497 A.2d 530 (N.J. Super. Ct. App. Div. 1985); Florence v. Merchs. Cent. Alarm Co., 412 N.E.2d 1317 (N.Y. 1980); Reed's Jewelers, Inc. v. ADT Co., 260 S.E.2d 107 (N.C. Ct. App. 1979); Fretwell v. Prot. Alarm Co., 764 P.2d 149 (Okla. 1988); Wedner v. Fid. Sec. Sys., Inc., 307 A.2d 429 (Pa. Super. Ct. 1973); Ostalkiewicz v. Guardian Alarm, 520 A.2d 563 (R.I. 1987); Underwood v. Nat'l Alarm Servs., Inc., No. E2006-00107-COA-R3-CV, 2007 WL 1412040 (Tenn. Ct. App. May 14, 2007); Arthur's Garage, Inc. v. Racal-Chubb Sec. Sys., Inc., 997 S.W.2d 803 (Tex. App. 1999); Jennings v. Brinks Home Sec., Inc., No. 22957-9-II, 1999 WL 615058 (Wash. Ct. App. Aug. 13, 1999).

93. 246 N.W.2d 443 (Minn. 1976).

94. *Id.* at 448.

95. *See id.*

rather than unreasonably large, damages.[96] Instead of applying the two-prong test to determine whether such a clause is a penalty,[97] the Restatement provides that unconscionability doctrine governs the clause's enforceability.[98] Some states expressly follow this approach. For example, in *Purcell Tire & Rubber Co. v. Executive Beechcraft, Inc.*,[99] the Supreme Court of Missouri adopted the Restatement's approach by holding that a clause fixing disproportionately large damages may be a penalty but that a clause fixing disproportionately small damages is subject to unconscionability analysis.[100]

Some courts, in addition to looking for the presence of procedural and substantive unconscionability, place great weight on policy considerations when determining whether a limitation-of-liability clause is enforceable.[101] Commonly cited policy factors include (1) the effect on prices of holding a party liable for damages greater than the contracted amount, (2) the uncertainty of liability exposure, and (3) the ability of one party to be in a better position than the other to purchase liability insurance.[102] An additional policy consideration provided by courts is whether the parties consciously allocated the risk of burglary to the customer rather than to the alarm service company.[103]

Overall, the general trend in most courts has been to interpret limitation-of-liability clauses in alarm service contracts in the same manner as exculpatory clauses, rather than liquidated damages clauses, and find that such clauses are not unconscionable or contrary to public policy.[104]

B. The Minority Rule: Limitation-of-Liability Clauses Are Enforceable Unless Void as Penalties

A minority of states, however, determine the validity of limitation-of-liability clauses using the penalty test—the same analysis used to determine whether liquidated damages clauses are unenforceable penalties. Among these states are Ohio and California. The controlling case in Ohio is

96. *Compare* RESTATEMENT (SECOND) OF CONTRACTS § 356 (AM. LAW INST. 1981) ("A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty."), *with id.* § 356 cmt. a ("A term that fixes an unreasonably small amount as damages may be unenforceable as unconscionable.").

97. *See supra* note 47 and accompanying text.

98. *See* RESTATEMENT (SECOND) OF CONTRACTS § 356 cmt. d. The U.C.C. adopts a similar approach, providing that limitations of liability that fail to provide "at least a fair quantum of remedy for breach" are subject to deletion as unconscionable. U.C.C. § 2-719 cmt. 1 (AM. LAW INST. & UNIF. LAW COMM'N 2014).

99. 59 S.W.3d 505 (Mo. 2001).

100. *See id.* at 510.

101. *See* Arthur's Garage, Inc. v. Racal-Chubb Sec. Sys., Inc., 997 S.W.2d 803, 810–11 (Tex. App. 1999) (ruling that policy reasons favored upholding a limitation-of-liability clause in an alarm service contract).

102. *See id.*

103. *See* Fireman's Fund Am. Ins. v. Burns Elec. Sec. Servs., Inc., 417 N.E.2d 131, 133 (Ill. App. Ct. 1980).

104. *See* Gen. Bargain Ctr. v. Am. Alarm Co., 430 N.E.2d 407, 411 (Ind. Ct. App. 1982) (citing twelve jurisdictions that have upheld limitation-of-liability clauses in alarm service contracts).

Samson Sales, Inc. v. Honeywell, Inc.,[105] in which the Supreme Court of Ohio held that a limitation-of-liability clause, which limited an alarm company's liability for damages caused by its negligence to $50, was an unenforceable penalty because the limitation was disproportionate to reasonably foreseeable damages and because damages were readily ascertainable.[106] In doing so, the court applied the same test it uses to determine the enforceability of liquidated damages clauses.[107]

The controlling case in California is *Better Food Markets*, in which a limitation-of-liability clause was upheld because it was a "reasonable endeavor by the parties to estimate a fair average compensation for any loss that may be sustained."[108] There, the California Supreme Court treated a provision that limited an alarm company's liability for damages caused by negligence to $50 as a liquidated damages provision.[109] Unlike the Ohio court in *Samson Sales*, however, the California court emphasized the impracticality or extreme difficulty of estimating damages *at the time of contracting* and opined that the greater the difficulty in estimating damages, the greater the range of estimates a court should uphold as reasonable.[110]

It is not unusual that the *Samson Sales* court refused to enforce the underliquidated damages clause while the *Better Food Markets* court upheld a nearly identical provision. Courts applying the penalty test to underliquidated damages clauses generate unpredictable results, and the outcomes of these cases do not seem to vary, as one might think they would, based on the disproportion between the liquidated damages and the actual damages.[111]

One rationale for applying a liquidated damages analysis to determine the enforceability of limitation-of-liability clauses in alarm service contracts—a rationale that favors finding such clauses unenforceable—was summarized well by Judge William F. Cercone, who dissented in *Wedner v. Fidelity Security Systems, Inc.*[112]:

> If the parties can escape their contractual provisions for liquidated damages because the amount stated is unreasonably disproportionate (either higher or lower) to the actual damages involved, there is no logical reason why the same test of reasonableness should not apply to a contractual limitation of liability. I would hold therefore, that a

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105. 465 N.E.2d 392 (Ohio 1984).

106. *Id.* at 394. In addition to requiring that damages be "uncertain as to amount and difficult [to] pro[ve]" for such a contract to be enforceable, the Ohio court also specified that the contract as a whole must not be manifestly unconscionable and that it must be the clear intention of the parties that damages would be limited to the expressed amount in the event of a party's negligence. *Id.* (quoting Jones v. Stevens, 146 N.E. 894, 895 (Ohio 1925)).

107. *See id.* at 393–94.

108. Better Food Mkts. v. Am. Dist. Tel. Co., 253 P.2d 10, 15 (Cal. 1953). *Contra id.* at 17 (Carter, J., dissenting) ("[T]he $50 provision bears no reasonable relation to any amount which might have been lost by a failure of the system to operate.").

109. *Id.* at 13–16 (majority opinion).

110. *Id.* at 14–15.

111. *See* Warren, *supra* note 8, at 908–09 (describing eleven cases in which underliquidated damages were enforced or not enforced without any discernable pattern).

112. 307 A.2d 429 (Pa. Super. Ct. 1973).

> contractual *limitation*, as well as a contractual *liquidation* of damages, is not binding where unreasonable and bearing no relation to the loss that would result from defendant's failure to fulfill the terms of its contract. The limitation in this case "to a sum equal in amount to the yearly service charge hereunder" was clearly unreasonable and arbitrary, bearing no relationship whatever to the damages flowing from defendant's breach. In my opinion this provision, whether viewed as one of liquidated damages or as a limitation of damages, should not be enforced.[113]

However, it is likely that courts apply a liquidated damages analysis to these provisions for a simpler reason. Recall that alarm service contracts often refer to their limitation-of-liability clauses as "liquidated damages."[114] It may be that some courts treat limitation-of-liability clauses as liquidated damages clauses solely because contracts designate them as such.[115]

C. Uncertain Jurisdictions: A Look at Connecticut

Some jurisdictions have yet to adopt a definitive test for how they enforce limitation-of-liability clauses in alarm service contracts. At least one jurisdiction—the District of Columbia—applies a liquidated damages analysis as well as an unconscionability analysis when determining the enforceability of these clauses.[116] As mentioned above, a Connecticut appellate-level court has yet to decide the matter.[117] Connecticut trial-level courts appear to adopt the minority rule of interpreting such provisions as liquidated damages clauses. Federal courts applying Connecticut law, however, have viewed identical provisions as exculpatory clauses and applied the unconscionability and public policy test adopted by the majority of state courts.

1. Federal Application of Connecticut Law

In *Leon's Bakery, Inc. v. Grinnell Corp.*,[118] the Second Circuit, applying Connecticut law, addressed the enforceability of a limitation-of-liability clause in a fire alarm system contract.[119] The court recognized that the Connecticut Supreme Court had not addressed the issue yet, so it looked to the law of other jurisdictions to determine that the clause was enforceable because it was not unconscionable.[120] The court also noted policy reasons to uphold the provision, observing that premises owners are in a better position to buy appropriate insurance for the property and that "limitations

113. *Id.* at 433 (Cercone, J., dissenting).

114. *See supra* notes 76–77 and accompanying text; *see also* Samson Sales, Inc. v. Honeywell, Inc., 465 N.E.2d 392, 393 (Ohio 1984); *Wedner*, 307 A.2d at 430–31.

115. *See* Warren, *supra* note 8, at 903–04 (arguing that courts engage in "sheer label application" by applying the penalty rule to underliquidated damages simply because litigants call these clauses "liquidated damages").

116. *See* Bargaintown of D.C., Inc. v. Fed. Eng'g Co. of Wash., D.C., 309 A.2d 56, 57 (D.C. 1973) (ruling that an alarm service contract was enforceable under both tests).

117. *See supra* note 91 and accompanying text.

118. 990 F.2d 44 (2d Cir. 1993).

119. *Id.* at 47–50.

120. *Id.* at 47–49.

on liability help keep alarm services affordable."[121] Subsequently, the U.S. District Court for the District of Connecticut has followed *Leon's Bakery*'s ruling on the enforceability of limitation-of-liability clauses in alarm system contracts, placing additional emphasis on the policy reasons for upholding these types of provisions.[122]

2. Connecticut Trial-Level Court Decisions

Since *Leon's Bakery*, Connecticut still has not issued any appellate-level rulings regarding whether limitation-of-liability clauses in alarm service contracts are interpreted as exculpatory clauses or liquidated damages clauses.[123] Connecticut trial-level courts (the Connecticut Superior Courts) have weighed in on the issue, though.[124] So far, Connecticut Superior Courts have viewed these limitations of liability as liquidated damages clauses and have applied a three-prong test to determine their enforceability, considering whether (1) the damages are uncertain or difficult to prove, (2) the parties intended to liquidate damages in advance, and (3) the amount is "reasonable because it is not greatly disproportionate to the amount of damages which the parties assumed at the time of their contract would be sustained if the contract were breached."[125] This test has been applied with mixed results.[126]

The reason why some limitation-of-liability clauses are enforceable under this test and why others are not has less to do with differences in the drafting of the contracts and more to do with how courts apply the first and third prongs of the test. For example, in *Forster v. Advanced Electronic Services, Inc.*,[127] the Superior Court of Connecticut held that a contract satisfied the first prong of the test (whether damages are uncertain or difficult to prove) because "[t]he defendant is not a property insurer and cannot be expected to know the value of a customer's home and belongings."[128] The *Forster* Court also found that the third prong (whether

121. *Id.* at 49 (quoting Sommer v. Fed. Signal Corp., 593 N.E.2d 1365, 1370 (N.Y. 1992)).

122. *See* Omni Corp. v. Sonitrol Corp., 476 F. Supp. 2d 125, 129 (D. Conn. 2007).

123. At least one case acknowledged this uncertainty. *See* Mattegat v. Klopfenstein, 717 A.2d 276, 280 (Conn. App. Ct. 1998) ("It is unclear whether . . . the parties' contract is a liquidated damages clause or a disclaimer of liability clause."). However, the clause at issue was found to be neither an enforceable liquidated damages clause nor an enforceable exculpatory clause. *Id.* It is still uncertain, then, how a Connecticut court will rule if a limitation-of-liability clause passes one test but fails the other.

124. *See* Forster v. Advanced Elec. Servs., Inc., No. X03CV010510854S, 2002 WL 31463511 (Conn. Super. Ct. Oct. 15, 2002); Wyer v. Sonitrol Sec. Sys. of Hartford, Inc., 738 A.2d 1179 (Conn. Super. Ct. 1999); Hartford Ins. v. ADT Sec. Sys., Inc., No. CV 980357149, 1999 WL 259688 (Conn. Super. Ct. Apr. 22, 1999).

125. *Wyer*, 738 A.2d at 1182–83; *accord Forster*, 2002 WL 31463511, at *4; *Hartford Ins.*, 1999 WL 259688, at *1.

126. *Compare Forster*, 2002 WL 31463511, at *4–5 (upholding a limitation-of-liability clause in an alarm service contract), *and Hartford Ins.*, 1999 WL 259688, at *2 (same), *with Wyer*, 738 A.2d at 1183 (finding a limitation-of-liability clause in an alarm service contract to be an unenforceable penalty).

127. No. X03CV010510854S, 2002 WL 31463511 (Conn. Super. Ct. Oct. 15, 2002).

128. *Id.* at *4.

the stipulated amount was greatly disproportionate to the amount of presumable loss from a breach of contract) was satisfied because "the [contract] price does not generally include a sum designed to anticipate the possible need to pay the purchaser the value of the property that the system is to protect."[129]

In contrast, the Superior Court of Connecticut held that a contract did not satisfy these two factors in *Wyer v. Sonitrol Security Systems of Hartford, Inc.*[130] under very similar circumstances. Regarding the first prong, the *Wyer* Court found that the value of the lost property was readily ascertainable and that an inventory of the property could have been conducted at the time of contracting.[131] Under the third prong, the actual damages ($6,800) were found to be greatly disproportionate to the liquidated damages ($198.44).[132]

As the conflicting federal and state rulings in Connecticut illustrate, the test to determine the enforceability of limitation-of-liability clauses in alarm service contracts, as well as the enforceability of the clauses themselves, is not settled law in all jurisdictions. Furthermore, jurisdictions like the District of Columbia that apply both tests may eventually encounter a case where a provision passes one test but fails the other,[133] forcing a decision as to which test actually is controlling.

III. AN OPPORTUNITY TO CRAFT A BETTER RULE

The uncertainty in some states provides an opportunity to address which rule courts should apply and, more generally, whether limitation-of-liability clauses in alarm service contracts should be enforced when an alarm service provider negligently fails to provide its bargained-for services. This part discusses the benefits of choosing one rule over the other by analyzing the implications each rule has for consumers, insurance companies, and the courts. Part III.A argues that limitation-of-liability clauses in alarm service contracts would be unenforceable penalties in jurisdictions that analyze such provisions as liquidated damages clauses. It also argues that adopting this rule would create perverse incentives for alarm service companies to redraft their contracts. Part III.B questions the conventional policy rationale provided by many courts for allowing alarm service providers to disclaim liability for negligence in limitation-of-liability clauses. Finally, Part III.C proposes adopting the majority rule of analyzing limitation-of-liability clauses as exculpatory clauses and contends that certain limitation-of-liability clauses in alarm service contracts should be void as a matter of public policy.

129. *Id.* at *5 (quoting Leon's Bakery, Inc. v. Grinnell Corp., 990 F.2d 44, 49 (2d Cir. 1993)).
130. 738 A.2d 1179 (Conn. Super. Ct. 1999).
131. *Id.* at 1183.
132. *Id.*
133. *See infra* Part III.A.

A. Perverse Incentives from Applying the Penalty Test

As an initial matter, it is worth noting that if limitation-of-liability clauses like the provision in *Better Food Markets* are interpreted as liquidated damages clauses, they should not pass the penalty test. This is primarily because, while the amount of damages might be difficult to estimate at the time of contracting, there is no reason to believe that damages flowing from an alarm service provider's negligence would be difficult for the nonbreaching party to prove.[134] In fact, property losses from theft, fire, or water damage are relatively simple to quantify.[135] These types of losses stand in contrast to damages that are more difficult to calculate, such as revenue losses from breaches of nondisclosure or nonsolicitation agreements.[136]

Moreover, the stipulated damages in alarm service contracts do not purport to be a reasonable estimate of anticipated or actual loss caused by a breach but instead fix an arbitrary amount, such as $50.[137] As it is not difficult to prove damages, courts should give very little deference to this fixed amount.[138] Additionally, it can hardly be said that this amount is designed to compensate the nonbreaching party for the other party's failure to perform.[139]

From this analysis, it appears that cases such as *Samson Sales* and *Wyer* correctly held that, when interpreted as liquidated damages clauses, limitation-of-liability clauses in alarm service contracts are not enforceable when they limit a service provider's liability to an unreasonably small amount for damages caused by the provider's own negligence. This reflects the general attitude that a plain underestimate of the probable loss from nonperformance of a contract is just as bad as an overestimate.[140] To consumers of alarm services, refusing to enforce underliquidated damages clauses might seem like a good policy. After all, if a plaintiff can prove that

134. *See supra* notes 47–50 and accompanying text.

135. *See* Samson Sales, Inc. v. Honeywell, Inc., 465 N.E.2d 392, 394 (Ohio 1984) (finding damages from the breach of an alarm service contract to be "as readily ascertainable as the damages in a multitude of other conceivable situations involving negligence and/or breach of contract"). *But see* Forster v. Advanced Elec. Servs., Inc., No. X03CV010510854S, 2002 WL 31463511, at *4 (Conn. Super. Ct. Oct. 15, 2002) (finding that the amount of fire damage that was specifically attributable to an alarm system's failure would be difficult to ascertain).

136. *See* Overholt Crop Ins. Serv. v. Travis, 941 F.2d 1361, 1370 (8th Cir. 1991) (enforcing a liquidated damages clause because damages from breaches of nondisclosure and nonsolicitation agreements are difficult to calculate).

137. *See* Better Food Mkts. v. Am. Dist. Tel. Co., 253 P.2d 10, 18 (Cal. 1953) (Carter, J., dissenting) ("The characteristic feature of a penalty is that it bears no relation to the actual damage which may be caused by a breach, but is arbitrarily fixed without any attempt to estimate the amount of injury."). Justice Jesse W. Carter, dissenting in *Better Food Markets*, suggested that the average amount of cash and inventory left in the store overnight would have been a reasonable estimate of damages. *Id.* at 17.

138. *See supra* note 50 and accompanying text.

139. *See generally* JKC Holding Co. v. Wash. Sports Ventures, Inc., 264 F.3d 459, 468 (4th Cir. 2001) (stating that liquidated damages clauses are "based on the principle of just compensation"); 24 WILLISTON & LORD, *supra* note 48, § 65:1.

140. *See* Fritz, *supra* note 8, at 202, 213–14.

an alarm company's failure to perform its contractual duty was the proximate cause of property loss from a burglary or fire, why should she be limited to recovering such a seemingly small, arbitrarily determined amount of damages?

At first glance, home and business owners might think that the Ohio Supreme Court's approach in *Samson Sales* and the Connecticut Superior Court's approach in *Wyer*—interpreting limitation-of-liability clauses as liquidated damages clauses—provides them with protection against unreasonable limitations of liability. However, alarm service consumers might be worse off under such an approach because alarm service providers might respond by redrafting their contracts to eliminate the fixed damage amount and completely disclaim liability altogether. By doing so, the limitation-of-liability clause would become an exculpatory clause instead.

Generally, exculpatory clauses are enforceable unless they are unconscionable or contravene public policy.[141] Exculpatory clauses that relieve a party from its own negligence, while disfavored, are upheld if expressed unambiguously and assented to by both contracting parties.[142] As this test focuses on different criteria than the penalty test does, a contract could potentially pass one test but fail the other. An unenforceable limitation-of-liability clause, stripped of its liquidated damages, could thus become an enforceable exculpatory clause.[143]

Consider, then, the ironic consequence of redrafting a contract to avoid a penalty test analysis: a previously unenforceable provision limiting damages to $1,000 may suddenly become enforceable when the amount is changed to $0. This perverse result reveals an inconsistency in jurisdictions that apply the penalty test to underliquidated damages but an unconscionability test to exculpatory clauses: if the law allows a party to assume the *entirety* of risk with no remedy whatsoever (as one does by agreeing to an exculpatory clause), there is no reason to deny a party the ability to assume a *part* of that risk instead (as one does by agreeing to a limitation-of-liability clause).[144]

Accordingly, treating limitation-of-liability clauses as liquidated damages clauses would create an incentive for alarm service providers to eliminate fixed damages provisions from their service contracts and replace them with complete disclaimers of liability for negligence. If these complete disclaimers are enforceable, then alarm service consumers would be worse

141. *See supra* Part I.A.

142. B & D Assocs., Inc. v. Russell, 807 A.2d 1001, 1005–06 (Conn. App. Ct. 2002); Mattegat v. Klopfenstein, 717 A.2d 276, 280 (Conn. App. Ct. 1998).

143. *Compare* Nahra v. Honeywell, Inc., 892 F. Supp. 962, 967 n.2 (N.D. Ohio 1995) (opining that an alarm service provider could "exculpate itself from all liability in an appropriately drafted contract"), *with* Samson Sales, Inc. v. Honeywell, Inc., 465 N.E.2d 392, 394 (Ohio 1984) (ruling that limiting liability to $50 constitutes an unenforceable penalty). *But see* Braden v. Honeywell, Inc., 8 F. Supp. 2d 724, 728–29 (S.D. Ohio 1998) ("[I]t is inconceivable that the Ohio Supreme Court would have refused enforcement of a clause limiting damages to $50.00 while at the same time would have enforced a clause preventing *any* liability under the same contract.").

144. *See* 11 JOSEPH M. PERILLO, CORBIN ON CONTRACTS § 58.16 (rev. ed. 2005).

off. After all, recovering an unreasonably small amount of damages from a service provider's negligence is better than being barred from seeking any damages whatsoever. Furthermore, reducing the cost of an alarm service provider's negligence is unlikely to encourage providers to take more care in installing and monitoring their systems.[145] This may result in a decrease in the quality of alarm systems.[146] Not only would alarm service consumers be worse off, but society would also receive a reduced benefit from any positive externalities that alarm services generate.[147]

The real issue then becomes whether these redrafted contracts that disclaim all liability for negligence would be enforceable, which depends on whether their exculpatory clauses are unconscionable or contrary to public policy.[148] Thus, applying the penalty test to limitation-of-liability provisions merely postpones the eventual determination of whether disclaimers of liability in alarm service contracts are unconscionable or against public policy. The underliquidated damages in cases like *Better Food Markets* were so unreasonably small in comparison to the actual losses that they were essentially token payments.[149] As a "mere token payment is as objectionable as eliminating it altogether,"[150] a jurisdiction might as well face the inevitable and determine whether limitation-of-liability clauses in alarm service contracts are unconscionable or against public policy.

Applying the penalty test to limitation-of-liability clauses in alarm service contracts may result in a short-lived victory for consumers. However, it might make consumers, insurers, and society worse off in the long run when alarm companies redraft their contracts to avoid the penalty test—unless, that is, the jurisdiction has ruled that complete disclaimers of liability for an alarm company's negligence are unconscionable or against public policy.

B. Questioning the Conventional Policy Wisdom

Having determined that analyzing the enforceability of limitation-of-liability clauses in alarm service contracts using the penalty test may not be the best approach,[151] the unconscionability and public policy analysis used to determine the enforceability of exculpatory clauses appears to be the obvious alternative. Under this analysis, courts generally find that such clauses are not unconscionable or against public policy.[152] However, there is reason to believe that the typical policy reasons for enforcing such clauses are misguided. An alarm company trade association's website

145. *See infra* Part III.B.1.
146. *See infra* Part III.B.1.
147. *See generally* Bruce L. Benson & Brent D. Mast, *Privately Produced General Deterrence*, 44 J.L. & ECON. 725, 729–31 (2001).
148. *See supra* Part I.A.
149. Recall that in *Better Food Markets*, liquidated damages were $50 while actual damages were over $35,000. *See supra* notes 2–4 and accompanying text.
150. Fritz, *supra* note 8, at 210.
151. *See supra* Part III.A.
152. 57A AM. JUR. 2D *Negligence* § 69 (2004).

provides an illustrative example. It asks the question "Why Won't You be Responsible for Your Own Negligence?" and answers with the following:

> This question is posed thousands of times a year to security companies. The answer is that the security company is not the cause of the loss. The burglar, robber, rapist, arsonist or other negligent party is the direct cause of the loss. Security companies can do no more than detect. The process of detection is not perfect. THERE WILL BE FAILURES, human or otherwise. The allocation of the cost of that risk to the security company would endanger the viability of the industry by creating exposures vastly disproportionate to the income derived.[153]

This answer reflects several commonly proffered arguments for enforcing limitations of liability in alarm service contracts: (1) that alarm companies are not the best insurers of their own failures and that holding otherwise would endanger the industry; (2) that the risk of burglary or fire is allocated to the customer, not the alarm company; and (3) that alarm companies are not responsible for losses caused by their own negligence because intervening tortfeasors are the direct cause of the losses. The following sections address these issues, respectively.

1. The Better-Insurer Argument

In *Leon's Bakery*, the Second Circuit placed significant emphasis on the idea that premises owners are in a better position to purchase appropriate insurance for lost or damaged property.[154] Placing such importance on the availability of insurance for premises owners, though, ignores a few realities of alarm service contracts. The first is that an individual estimate of potential losses from burglaries or fires probably would not be overly burdensome to include in an alarm service contract because the company needs to visit the premises to install the alarm service in the first place. This level of individual interaction with the customer gives the alarm service company an opportunity to gather information about the customer. Alarm companies could price discriminate based on whether the alarmed premises is a home or business. Within these categories, alarm companies could further discriminate based on neighborhood affluence or business type.

The second reality is that emphasizing the ability of premises owners to obtain insurance ignores the fact that liability insurance is available for alarm service providers as well.[155] These insurers would presumably raise

153. *Limitations of Liability*, CENT. STATION ALARM ASS'N INT'L, http://csaaintl.org/issues/limitations-of-liability/#Why%20Won't%20You%20be%20Responsible%20for%20Your%20OOO%20Negligence? (last visited Oct. 16, 2016) [https://perma.cc/2DUF-K58M].

154. *See supra* note 121 and accompanying text.

155. *See Alarm Contractors Business Insurance*, HARTFORD, https://www.thehartford.com/business-insurance/alarm-contractor (last visited Oct. 16, 2016) [https://perma.cc/2KNH-R42L]; *Alarm Contractors Insurance / Installers / Security Company*, ALLRISKS, http://www.allrisks.com/industry-specialties/detail/alarm-companies (last visited Oct. 16, 2016) [https://perma.cc/E3WY-CKAV]; BROWNYARD PROGRAMS, http://www.brownyardprograms.com/ (last visited Oct. 16, 2016) [https://perma.cc/N4GZ-WZCN].

or lower insurance rates for alarm service providers based on the rate at which their service fails because of the provider's negligence.

However, the incentive for an alarm service provider to reduce its negligence rate is not present if the provider is able to exculpate itself from liability.[156] This is because the nature of contract "is optional: a party can either do a promised thing or pay damages."[157] Accordingly, an alarm service provider has an incentive to spend only the amount of money that is "just worth it" to guard against its own negligence.[158] Where an alarm service provider is able to exculpate itself from liability, that amount is equal to the underliquidated damages provision. This amount is not "efficient," though, because the compensation does not mirror the value of full performance.[159] As this Note has discussed at length, the damages from an alarm company's negligence often far exceed the underliquidated damages provision.

Furthermore, alarm service providers are likely the least-cost insurers of damages from their own negligence in these scenarios because they are in control of their own negligence rate.[160] The cost of insuring against damages from an alarm company's negligence would consist of two main expenses: (1) the expected value of the underwriting loss to the insurer and (2) transaction costs, such as the cost of determining the probability of nonperformance and the cost of negotiation and communication with the insured.[161] Here, the alarm company has an advantage over a third-party insurer. The cost of negotiation and communication with the insured will be similar for alarm companies and third-party insurers alike, but the alarm

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156. *See* Burnham, *supra* note 9, at 381 (noting that "exculpation undermines the deterrent effect of tort liability"). Judge Richard A. Posner criticized this idea in *Edwards v. Honeywell, Inc.*, 50 F.3d 484 (7th Cir. 1995), where he opined:

> Pointing to the $250 limitation of the alarm service's liability to the [homeowners], the plaintiff argues that if Honeywell prevails in this suit, alarm services will have no incentive to take care. But they will. Honeywell lost the [homeowners'] business. Our society relies more heavily on competition than on liability to optimize the quality of the goods and services supplied by the private sector of the economy. A case such as this does Honeywell's customer relations no good even if it wins the case . . . .

Id. at 491. However, Judge Posner's approach, which requires a consumer to "shop around and perhaps forego the activity, may not adequately protect consumers from exculpatory clauses in modern business dealings." Guissinger, *supra* note 9, at 800. Competition may not adequately protect consumers from exculpatory clauses because (1) markets might be monopolistic rather than competitive, (2) inadequate information may be available to consumers, and (3) boilerplate language only becomes important when something goes wrong. *See id.* at 800 n.35 (citing Arthur Allen Leff, *Unconscionability and the Crowd—Consumers and the Common Law Tradition*, 31 U. PITT. L. REV. 349, 351 (1970)).

157. Warren, *supra* note 8, at 915.

158. *See* Goetz & Scott, *supra* note 10, at 581.

159. *See id.* at 558.

160. *See id.* at 583 ("[T]here are strong economic arguments that suggest that the vendor is the lowest-cost insurer against non-performance . . . [when] the vendor has some control over the probability of externally caused non-performance.").

161. *See id.* at 579–80.

company is in a superior position to know the probability that it will negligently fail to perform its service.[162]

More importantly, the alarm company is able to exercise some control over the rate at which it will negligently fail to perform its service.[163] Thus, the alarm company is in a unique position to reduce the expected value of the underwriting loss by taking steps to reduce its negligence rate.[164] The alarm company would therefore have an incentive to spend resources to decrease its negligence rate up to the point where it is "just worth it."[165] Hence, even if the alarm company would incur the same transaction costs as a third-party insurer, the alarm company has an efficiency advantage.[166] As between an alarm service customer, the customer's third-party insurer, and an alarm service company, net welfare would increase if alarm companies were required to insure against their own negligence.

For example, suppose that a customer purchases third-party liability insurance and an alarm service and pays $2,000 a year for each contract. Part of the price of the third-party liability insurance is the risk that losses may occur from the alarm company's negligence—say, $200 of the contract price. Now assume the alarm service company is liable for losses caused by its own negligence. The alarm company will now have an incentive to reduce its negligence rate and will increase the cost of its service to account for its increased liability. Supposing the alarm company halved its negligence rate, the new alarm contract price would be $2,100. However, the third-party insurer no longer has to insure against the risk of the alarm company's negligence, so it would be able to reduce its price to $1,800. This results in a net welfare increase of $100.

The upshot is that consumers will end up paying less in total for property insurance and alarm services because alarm companies will take steps to reduce the rate of their negligence. Not only does this benefit consumers, but the reduction in burglary and fire losses presumably benefits society as a whole. Consumers should be willing to pay the higher prices alarm service companies would have to charge to compensate for their increased liability because of the lower property insurance prices and increase in the quality of alarm services. This strongly calls into question the contention that an increase in liability would make alarm services prohibitively costly.

While courts cite the availability of third-party liability insurance as a policy reason in support of enforcing limitation-of-liability clauses in alarm service contracts, a detailed analysis of the party that is *actually* in the best position to insure against an alarm company's negligence reveals that society as a whole would benefit if alarm companies were liable for their own negligence. Accordingly, public policy favors finding these clauses unenforceable.

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162. *See id.* at 580.
163. *See id.*
164. *See id.*
165. *See id.* at 581.
166. *See id.* at 582.

2. The Risk-Allocation Argument

As an additional policy reason to enforce limitation-of-liability clauses in alarm service contracts, some courts find that these provisions represent the parties' decision to consciously allocate the risk of burglary or fire to the customer rather than to the alarm service company.[167] One court noted that "[f]or the small compensation received obviously [the alarm company] could not afford to assume responsibilities such as are assumed in the case of fire insurance coverage."[168] Another court opined that holding an alarm service company liable for damages caused by its negligence "would in practical effect excuse the homeowner from having to insure the property and would shift the risk of its loss to the burglar alarm manufacturer."[169]

These fears of requiring alarm service companies to become general casualty insurers are misplaced. The plaintiffs in the cases cited by this Note were not contending that alarm service providers should be liable for *all* burglaries and fires. Rather, they are simply arguing that alarm service providers should be liable for losses *caused by the alarm company's own negligence*. Thus, if a burglar breaks into a store and the alarm company alerts the police according to the terms of its contract, the alarm company would not be liable simply because the police fail to catch the burglar. The scenario at issue is where the alarm company negligently fails to alert the police *and* the plaintiff can prove that the alarm company's failure to perform its contractual duty was the proximate cause of her loss—as was the case in *Better Food Markets*.[170]

Alarm service providers are not being asked to become insurers against burglaries or fires. They are being asked to become insurers against their own negligence. As alarm companies are the least-cost insurers of their own negligence,[171] it is in society's best interest to expect them to bear this burden.[172]

3. The Intervening-Tortfeasor Argument

Another policy issue some courts raise when deciding a limitation-of-liability clause's enforceability is the difficulty in calculating an alarm company's portion of liability for losses caused by an intervening

167. *See* Fireman's Fund Am. Ins. v. Burns Elec. Sec. Servs., Inc., 417 N.E.2d 131, 133 (Ill. App. Ct. 1980); *see also* Warren, *supra* note 8, at 932–33 (describing the perception that "underliquidated damages provisions were frequently the result of deliberate risk allocation").

168. Atkinson v. Pac. Fire Extinguisher Co., 253 P.2d 18, 21 (Cal. 1953).

169. Lobianco v. Prop. Prot., Inc., 437 A.2d 417, 424 (Pa. Super Ct. 1981).

170. *See supra* note 2 and accompanying text.

171. *See supra* Part III.B.1.

172. Though not *desirable*, should it nevertheless be *permissible* for alarm companies to contract away liability for their own negligence? Part III.C, *infra*, answers this question in the negative.

tortfeasor.[173] An intervening tortfeasor is an actor who brings about harm after another's negligent act or omission.[174] Applied to burglar alarm service failures, a burglar is an intervening tortfeasor who causes harm after an alarm company's negligent failure to call the police. Recall that one policy justification provided by the alarm service trade association's website was that "the security company is not the cause of the loss. The burglar, robber, rapist, arsonist or other negligent party is the direct cause of the loss."[175]

Despite an intervening tortfeasor being the direct cause of the loss, another actor's negligence will create liability if "the actor at the time of his negligent conduct realized or should have realized the likelihood that such a situation might be created, and that a third person might avail himself of the opportunity to commit such a tort or crime."[176] When it comes to an alarm service company's negligent failure to provide its service, it is obvious that the company realized or should have realized the likelihood of losses caused by a third person's criminal act, as such crimes were expressly contemplated during contract formation. Indeed, the court in *Central Alarm of Tucson v. Ganem*[177] noted that "[i]t is hard to imagine circumstances more appropriate than those before us, where the only reason for installation and maintenance of the alarm system was the foreseeability of a possible burglary attempt."[178] Accordingly, the foreseeability of damages caused by a burglar if an alarm service negligently fails to provide its contractual obligations means that alarm companies are still liable even if the burglar is the direct cause of the loss.[179]

On close inspection, the public policy arguments typically cited in support of enforcing limitation-of-liability clauses in alarm service contracts are unconvincing. While it is true that customers can purchase third-party liability insurance to cover the risk of alarm companies negligently failing to provide their services, alarm companies themselves

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173. *See* Warren, *supra* note 8, at 913 n.80 ("[S]ome courts note the difficulty of litigating how much the failure of the alarm system increased the loss from fire or burglary.").

174. *See* RESTATEMENT (SECOND) OF TORTS § 441 (AM. LAW INST. 1965).

175. *Limitations of Liability*, *supra* note 153.

176. *See* RESTATEMENT (SECOND) OF TORTS § 448.

177. 567 P.2d 1203 (Ariz. Ct. App. 1977).

178. *Id.* at 1206 (citations omitted). The *Ganem* court went on to find that the burglary "was certainly within the ambit of risk" created by the alarm company's failure and that, but for the alarm company's negligence, "the loss would not have occurred approximately 99 times out of 100, based on the success rate of a properly maintained system." *Id.* at 1206.

179. *Cf.* Monitronics Int'l, Inc. v. Veasley, 746 S.E.2d 793, 801 (Ga. Ct. App. 2013) (finding that an alarm company was the proximate cause of the plaintiff's injuries when she was sexually assaulted by an intruder). The precise manner in which liability should be apportioned is beyond the scope of this Note. However, any difficulty in calculating damages seems like a slender reed to rest an argument against holding alarm service providers accountable for damages they proximately caused, especially considering the willingness of courts to apportion liability—despite intervening tortfeasors—in other areas of the law. *See generally* E.L. Kellett, Annotation, *Private Person's Duty and Liability for Failure to Protect Another Against Criminal Attack by Third Person*, 10 A.L.R.3d 619 (1966).

would be the most efficient insurers of their own negligence. Imposing this liability on alarm companies would not force companies to assume a customer's general casualty risks. Instead, it would incentivize companies to reduce their negligence rates by forcing them to account for the consequences of their mistakes. Finally, as the consequences of an alarm company's failure to provide its services are foreseeable, such a failure would be the proximate cause of a customer's damages even if a burglar or an unattended stove is the direct cause of the loss.

C. A New Public Policy Approach

While it traditionally has been employed to enforce limitation-of-liability clauses in alarm service contracts, the unconscionability and public policy test is still the best approach for courts to adopt because it provides courts with the flexibility to protect consumers from particularly egregious limitation-of-liability clauses.

Courts should rule that underliquidated damages clauses in alarm service contracts that provide nominal damages in gross disproportion to actual damages are substantively unconscionable. It is commonplace for service contracts to disclaim consequential damages by limiting liability to the cost of the service.[180] By doing so, even though the customer is denied her traditional expectancy remedy under contract law, she is at least able to protect her restitution interest. Alarm service contracts that limit liability to unreasonably small damages in the event of an alarm company's negligence deny the customer her expectancy *and* restitution interest. Imagine how this provision would read in any other service contract: "We will charge you $1,250 for our services. If, through our own failure to exercise ordinary care, we fail to provide those services, your damages are limited to $250." Such a contract seems absurd. Its terms are "so oppressive that no reasonable person would make them and no fair and honest person would accept them."[181] In other words, it is substantively unconscionable. Nevertheless, this is essentially what courts are enforcing when they uphold limitation-of-liability clauses in alarm service contracts.

Courts should not enforce limitation-of-liability provisions in alarm service contracts that ignore all remedies under contract law. If a customer cannot be put in the position she would have been in had the alarm service company provided its service, she should at least be able to be put in her precontract position. Otherwise, the alarm company has made the customer worse off than she was before. However, the continuous relationship between alarm service providers and customers makes restitution

180. *See* Metro. Prop. & Cas. Ins. v. Pest Doctor Sys., Inc., No. 3:14-CV-143, 2015 WL 4945767, at *4 (S.D. Ohio Aug. 20, 2015) ("To the fullest extent permitted by law, [the service company] will not be liable for personal injury, death, property damage, loss of use, loss of income or any other damages whatsoever, including consequential and incidental damages, arising from this service. [The service company's] liability is specifically limited to the labor and products necessary to [perform the service].").

181. Burnham, *supra* note 9, at 384.

problematic.[182] A viable alternative, then, is to protect the customer's expectancy interest by refusing to enforce the unconscionable provision and allowing the customer to proceed with her underlying claim for actual damages.

On the public policy side, courts would be free to demand that, to be enforceable, limitation-of-liability clauses must better compensate the nonbreaching party—especially after recognizing that the traditional policy rationales for enforcing limitation-of-liability clauses in alarm service contracts no longer provide sufficient justifications for shifting the burden of an alarm service provider's negligence onto the consumer.[183] From an efficiency perspective, social policy dictates that alarm service providers should not be able to disclaim liability for negligently failing to provide their services, because they are likely to be the least-cost insurers of their own negligence.[184]

In the majority of states, the policy of freedom of contract typically outweighs other policies, with the exception of areas of public interest.[185] "Freedom of contract is generally believed to be a good thing. And so is the concept that one who acts negligently should be held responsible for the injury caused by his or her act."[186] In the context of alarm service contracts, holding alarm companies accountable for damages caused by their negligence is an area of public interest courts should consider. Enforcing underliquidated damages clauses in alarm service contracts creates an incentive for alarm service providers to pay a nominal fee rather than spend the appropriate level of resources to reduce the rate of their own negligence.[187] Here, the social interest in avoiding the needless waste associated with the inefficient use of resources "may be great enough that freedom to limit liability for negligent injury to another's . . . property should be curtailed."[188] The question, then, is whether this social objective is "important enough that individuals should not be permitted to interfere with them by shifting the incidence of risks"[189] and whether the courtroom is an appropriate place to make this determination.

Public policy has been described as "a very unruly horse, and when once you get astride it you never know where it will carry you."[190] Some have argued that a court cannot properly weigh the advantages and disadvantages of such policy decisions because the "primary function of a court is to resolve the specific dispute before it."[191] Thus, "[u]nlike a legislature, a

182. *See supra* Part I.C.2.
183. *See supra* Part III.B.
184. *See supra* Part III.B.1.
185. Burnham, *supra* note 9, at 390.
186. *Id.* at 379.
187. *See supra* Part III.B.1.
188. Fritz, *supra* note 8, at 222.
189. *Id.*
190. Richardson v. Mellish (1824) 130 Eng. Rep. 294, 303.
191. Guissinger, *supra* note 9, at 802; *see* Jonathan Cohen, Note, *Judicial Control of the Purse—School Finance Litigation in State Courts*, 28 WAYNE L. REV. 1393, 1416 (1982)

court cannot hold open hearings, inviting testimony as to costs, risks, etc., from all interested parties."[192] Accordingly, matters of public interest might be addressed more effectively by legislatures rather than by courts.[193]

Indeed, the New York State Legislature has prohibited the owners of pools, gymnasiums, places of amusement or recreation, or similar establishments from disclaiming their liability for damages caused by the owner's negligence, declaring such limitations of liability "void as against public policy and wholly unenforceable."[194] A legislature could similarly declare limitations of liability for damages caused by an alarm company's negligence to be void as a matter of public policy. A state-by-state legislative solution has the additional appeal of allowing elected representatives, rather than judges, to make the determination of whether freedom of contract outweighs the importance of holding negligent parties accountable for the injuries they cause. This decision may differ based on the ideals of the citizenry in each state.

A legislative solution also may have benefits in terms of certainty.[195] Clear rules regarding liability would allow alarm service companies to price their services to reflect their exposure to liability. The alarm-company-as-best-insurer-of-its-own-negligence argument works only if the alarm company knows about its liability in advance so that it can price its service accordingly. Additionally, the efficiency benefits from the alarm company acting as the least-cost insurer may be reduced if liability is excessively litigated after every incident. A clear public policy statement from a state's legislature regarding the enforceability of limitations of liability for an alarm company's negligence could curtail litigation by making the outcome of these lawsuits more certain.

Overall, the extreme discrepancy between actual damages and underliquidated damages in a typical case where an alarm company negligently fails to provide its contractual services, along with the efficiency and public policy gains from holding alarm companies liable for their own negligence, favor finding limitation-of-liability clauses in alarm service contracts unconscionable and contrary to public policy. Applying an unconscionability and public policy test strikes at the heart of the matter—whether these clauses are too unfair to enforce—rather than creating loopholes, and it provides the additional benefit of allowing state legislatures to weigh in on the matter.

(discussing how "[r]emedies are granted on a case-by-case basis," while "legislatures traditionally focus on the problems of society as a whole").

192. Guissinger, *supra* note 9, at 802.

193. *Id.* at 802–03; *see* DONALD L. HOROWITZ, THE COURTS AND SOCIAL POLICY 23 (1977) ("[M]any aspects of adjudication that seem well suited to the determination of particular controversies seem unsuited to the making of general policy.").

194. N.Y. GEN. OBLIG. LAW § 5-326 (McKinney 2012).

195. *See* HOROWITZ, *supra* note 193, at 37 (describing how the "piecemeal quality of judicial decisions" can "unsettle old patterns without providing unambiguous new patterns to which expectations can conform").

CONCLUSION

Limitation-of-liability clauses in alarm service contracts present a unique challenge for courts. Unlike exculpatory clauses in contracts for recreational activities, which relieve a party from liability for damages caused by negligence *while* providing a service, limitation-of-liability clauses in alarm service contracts limit an alarm company's liability for negligently failing to *provide* bargained-for services. However, unlike a true liquidated damages provision, limitation-of-liability clauses do not purport to estimate the harm caused by nonperformance. How, then, should courts determine their enforceability? Should they be enforced at all?

A policy that refuses to enforce limitation-of-liability clauses in alarm service contracts on the basis that they are unenforceable penalties may simply create a loophole to be exploited by clever drafting. Ultimately, the real question is whether these provisions are unconscionable or void as a matter of public policy. As a market exists for alarm services, courts are unlikely to find these provisions procedurally unconscionable. However, the conventional explanations for why limitation-of-liability clauses are not substantively unconscionable or contrary to public policy are unconvincing. Refusing to enforce these clauses would not force alarm companies to become general casualty insurers. Rather, alarm companies would be insurers only against their own negligence. As alarm companies themselves—not third-party insurers—are the least-cost insurers of their own negligence, holding alarm companies accountable for their own negligence would advance public policy interests.

While freedom of contract is an important concept, so is the notion that a party should be held accountable for negligently injuring others. When these two concepts conflict, public policy considerations may tip the scales in favor of one or the other. Here, the obligation of care owed by alarm service companies to their customers outweighs the traditional regard for freedom of contract. When it comes to provisions in alarm service contracts that limit an alarm company's liability for damages caused by its own negligence, public policy favors holding alarm companies responsible for their negligence.