Consumers and Remedies: Do Limitation of Liability Clauses Do More Harm than Good

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CONSUMERS AND REMEDIES:
DO LIMITATION OF LIABILITY CLAUSES DO MORE HARM THAN GOOD?

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I. INTRODUCTION

The purchase of a home is at the heart of the American dream. This step in the life of the average American entails much uncertainty, as prospective homeowners rely on the expertise of many different facilitators when they set out to make their largest investment. For some homeowners, the dream turns into a nightmare because the home is fraught with construction defects, termite damage, or a crumbling foundation.¹ The nightmare is even worse if a home inspection report claimed the home had no defects.

Unfortunately for the homeowner, upon seeking out the inspector for an explanation, all the inspector may offer is a denial of any wrongdoing; the return of the fee paid; and a reminder that, under the home inspection contract, the inspector is liable only for the return of his fee.² The new homeowner would then face thousands of dollars in unexpected repairs to the home, while the home inspector walks away as if the contract never existed. The home inspector can escape accountability for failing to report the issues to the buyer. Additionally, while the inspector will be restored to his original position before entering into the agreement, the homebuyer will face thousands of dollars in home repairs. Is the law fair when it allows this result, letting service providers—such as home inspectors—perform poor work and then escape from liability for their negligence?

¹. This hypothetical scenario is based on Gladden v. Boykin, 402 S.C. 140, 739 S.E.2d 882 (2013).
². See, e.g., id. at 142 n.1, 739 S.E.2d at 883 n.1 (reviewing a limited liability clause that only allowed for the return of a home inspection fee in case of breach).
Under current South Carolina law, a limitation of liability provision—like in the home inspection contract described above—is enforceable, unless the provision is unconscionable or conflicts with public policy. The courts’ determination of unconscionability depends on several factors, including—but not limited to—the bargaining positions of the parties, the subject matter of the contract, and the visibility of the limitation of liability clause. To determine if the clause violates public policy, courts will look to whether the contract concerns a public interest. If the clause concerns a public interest and conflicts with the public policy related to that interest, courts will hold that the clause is unenforceable.

In South Carolina, the current method for determining the enforceability of limitation of liability provisions in contracts fails to provide reliable guidance for drafting or interpreting these common provisions. The multitude of factors involved, as well as the fact-intensive analysis needed to determine conflicts with public policy and unconscionability, result in inconsistent decisions and an unreasonably high barrier for parties attempting to challenge such clauses. To provide reliable guidance, the law in South Carolina needs a consistent test for determining the enforceability of a limitation of liability provision in consumer contracts for services. Specifically, courts should adopt the balancing test used for determining the enforceability of liquidated damages clauses for limitation of liability provisions. Adopting this test to analyze limitation of liability provisions would provide efficient determination of enforceability, while adhering to public policy interests and voiding unconscionable clauses in contracts.

This Note discusses the use of limitation of liability clauses in South Carolina and proposes changes to the courts’ analysis of these clauses. Part I discusses the state of the law in South Carolina regarding damage limiting clauses in contracts and the general effect of damage limiting clauses. Part II explains limitation of liability clauses and the tests used to determine their enforceability. Part III discusses liquidated damages clauses and the balancing test used to determine whether they are enforceable. Part IV proposes a new test to determine the enforceability of limitation of liability clauses that will not only ease the burdens placed on consumers by these clauses, but also provide for a more efficient determination of enforceability.

3. See, e.g., id. at 146, 739 S.E.2d at 885 (concluding that a limitation of liability provision in a home inspection contract was enforceable, as it was neither unconscionable nor did it violate public policy).
4. See id. at 145–46, 739 S.E.2d at 885.
5. See id. at 155, 739 S.E.2d at 890 (Beatty, J., dissenting) (quoting Pride v. S. Bell Tel. & Tel. Co., 244 S.C. 615, 620, 138 S.E.2d 155, 157 (1964)).
6. See id. at 159, 739 S.E.2d at 892.
7. See, e.g., id. at 150, 739 S.E.2d at 887 (“[T]here is no hard and fast definition of unconscionability and...it is an amorphous concept.” (quoting Lucier v. Williams, 841 A.2d 907, 911 (N.J. Super. Ct. App. Div. 2004))).
II. CONTRACT PROVISIONS ALTERING TRADITIONAL CONTRACT LIABILITY

A. The Clauses Explained

One type of liability altering clause is a limitation of liability clause, which caps the amount of one party’s or both parties’ liability under the contract. Limitation of liability clauses in contracts are so common today that most consumers regularly enter into agreements in which the consumer’s remedy is severely limited. In most instances, the limitation of liability clause goes unnoticed by the consumer and exists only to allow the service provider to cap its potential losses from the multiple contracts to which the service provider is a party. The consumer and the service provider rarely negotiate the limitation of liability clause; instead, the service provider typically drafts the agreement and presents it to the consumer on a take-it-or-leave-it basis. Furthermore, in the event of a breach of the contract between the consumer and the service provider, the limitation of liability clause becomes the consumer’s nightmare and the service provider’s sigh of relief.

The limitation of liability clause does not foreclose a party’s cause of action under the contract, nor does it eliminate either party’s liability; rather, the clause “guarantees only that a party will not be held liable for damages above a specified ceiling.” These clauses allow contracting parties to negotiate the amount of liability under the contract and anticipate the potential losses in the event of a breach. This method of negotiated liability allows for more efficient business transactions because the clause prepares the parties for any potential losses and the parties know the specific amount of potential liability. Efficiency results when both parties understand the limitation of liability clause and the potential impact of the clause. The impact of the clause is especially


9. See, e.g., Gladden, 402 S.C. at 144, 739 S.E.2d at 884 (“Limitation of liability . . . clauses are routinely entered into.”).

10. See, e.g., id. at 149, 739 S.E.2d at 886 (Beatty, J., dissenting) (suggesting that the consumer was likely not advised of the presence of the limitation of liability clause); see also Gwyn, supra note 8, at 61 (citing Valhal Corp. v. Sullivan Assoc., 44 F.3d 195, 202 (3d Cir. 1995); Fox & Wolff, supra note 8, at 408; JUSTIN SWEET, LEGAL ASPECTS OF ARCHITECTURE, ENGINEERING, AND THE CONSTRUCTION PROCESS 731–33 (4th ed. 1984)).

11. See Gladden, 402 S.C. at 147, 739 S.E.2d at 885–86 (Beatty, J., dissenting) (quoting Simpson v. MSA of Myrtle Beach, Inc., 373 S.C. 14, 26–27, 644 S.E.2d 663, 669 (2007)) (determining that the home inspection contract was a contract of adhesion and defining a contract of adhesion).

12. Gwyn, supra note 8, at 61 (citing Fox & Wolff, supra note 8, at 408).

13. See id. (citing STEVEN G.M. STEIN, CONSTRUCTION LAW 11–69 (1986)).

14. See id.

15. See id.
relevant to consumer contracts for services where the consumer is likely an unsophisticated party and, thus, unaware of the provision limiting the potential recovery in the event of the service provider’s breach.\(^\text{16}\)

Limitation of liability clauses are, however, distinguishable from indemnity provisions and exculpatory clauses in contracts.\(^\text{17}\) While all of the clauses serve a damage limiting function, each clause operates differently.\(^\text{18}\) Indemnity provisions, rather than reducing or eliminating a party’s liability, shift the liability from the indemnitor to the indemnitee.\(^\text{19}\) In other words, one party is contractually obligated to defend or pay for harm caused by another party.

Conversely, exculpatory clauses completely eliminate one party’s liability to the other in a contractual agreement.\(^\text{20}\) Courts have upheld exculpatory clauses in South Carolina, but “[s]ince such provisions tend to induce a want of care, they are not favored by the law and will be strictly construed against the party relying thereon.”\(^\text{21}\)

Although limitation of liability and exculpatory clauses are technically distinct, courts in South Carolina seem to use the terms interchangeably.\(^\text{22}\) Thus, South Carolina courts apply the same reasoning and precedent to both limitation of liability clause and exculpatory clause cases.\(^\text{23}\)

**B. South Carolina’s Interpretation of Limitation of Liability Clauses**

South Carolina courts generally uphold limitation of liability clauses in contracts to protect the private parties’ right of freedom of contract.\(^\text{24}\) However, limitation of liability clauses are subject to challenge on two main theories: unconscionability and conflict with public policy.\(^\text{25}\) These two challenges hardly create black letter rules, leading to many disputes being decided on a fact-

\(^{16}\) See, e.g., Gladden, 402 S.C. at 149, 739 S.E.2d at 886 (Beatty, J., dissenting) (describing that the consumer was likely not advised of the presence of the limitation of liability clause).

\(^{17}\) Gwyn, supra note 8, at 61.

\(^{18}\) See id.

\(^{19}\) See id.

\(^{20}\) See id.


\(^{23}\) See, e.g., id. at 294–95, 584 S.E.2d at 152 (citing Huckaby, 276 S.C. 629, 281 S.E.2d 223; Pride, 244 S.C. 615, 138 S.E.2d 155) (relying on limitation of liability precedent to discuss an exculpatory agreement).

\(^{24}\) See id. (citing Huckaby, 276 S.C. 629, 281 S.E.2d 223; Pride, 244 S.C. 615, 138 S.E.2d 155); Pride, 244 S.C. at 619, 138 S.E.2d at 157.

intensive, case-by-case basis. Unfortunately, this approach leaves practically no guidance to legal practitioners on how to draft effective and enforceable limitation of liability clauses. Furthermore, challenges based on conflicts with public policy and unconscionability create large hurdles for consumers that typically leave consumers without an adequate remedy.

In contractual agreements between consumers and service providers, the parties to the contract must have realistic motives to act diligently in carrying out their respective duties. Excessively limited damages reduce the parties’ motives to carry out their duties in this manner. Parties typically face the following motivations: payment for completing the contract, the benefit of the completed bargain, and the potential liability for breaching the contract. Frequently, the party drafting the agreement—usually the service provider—will include a limitation of liability clause that caps its potential damages if the provider breaches the contract. This standard practice reduces the transaction costs of the contract by providing a method for the parties to anticipate the potential losses in the event of breach. These clauses, however, are usually so broad that they essentially eliminate liability on behalf of the party seeking enforcement of the clause and provide only nominal recovery to the consumer.

To remedy this problem, courts should utilize the balancing test for liquidated damages clauses outlined in the Restatement (Second) of Contracts—which South Carolina courts have adopted—to determine the enforceability of limitation of liability provisions. The Restatement’s test determines the enforceability of liquidated damages clauses by balancing the reasonableness of the estimate of damages at the time of contract formation with the actual damages a party suffered. In applying this test, a court would need to focus on whether, at the time of contracting, the limitation of liability clause was a

26. See, e.g., id. at 148, 739 S.E.2d at 886 (Beatty, J., dissenting) (emphasizing the “importance of a case-by-case analysis” of limitation of liability clause litigation (quoting Simpson v. MSA of Myrtle Beach, Inc., 373 S.C. 14, 36, 644 S.E.2d 663, 674 (2007))).
27. See, e.g., id. at 146, 739 S.E.2d at 885 (majority opinion) (holding, after minimal discussion, that a limitation of liability provision in a home inspection contract was neither unconscionable nor did it violate public policy).
29. See generally Rebecca Hollander-Blumoff, Intrinsic and Extrinsic Compliance Motivations: Comment on Feldman, 35 WASH. U. J.L. & POL’Y 53 (2011) (discussing the intrinsic and extrinsic motivations that may exist to compel parties to comply with the law).
30. See Gwyn, supra note 8, at 61 (citing STEIN, supra note 13).
31. See id.
32. See, e.g., Murray v. Tex. Co., 172 S.C. 399, 402–03, 174 S.E. 231, 232 (1934) (reviewing a limitation of liability clause that was overly “broad and comprehensive”).
genuine, reasonable allocation of prospective loss in the event of breach. Next, the court would compare the estimate of loss provided in the limitation of liability clause to the actual loss the consumer suffered. The comparison of the estimate of loss to the actual loss suffered is balanced against the relative difficulty in determining the prospective loss at the time of contracting. If the prospective loss was impossible to determine at the time of contracting, the court should defer to the intent of the parties. If, however, the prospective loss was relatively easy to determine at the time of contracting, then the court should compare the clause precisely with the actual harm suffered. In other words, the more difficult it is to estimate the loss, the more likely it is that a court will find the limitation clause enforceable.

III. LIMITATION OF LIABILITY CLAUSES

A. Limitation of Liability Clauses in South Carolina

Currently, under South Carolina law, courts invalidate limitation of liability clauses in consumer service provider contracts when the clause is either unconscionable or violates public policy.

With regard to the enforceability of limitation of liability clauses, South Carolina law defines unconscionability as “the absence of meaningful choice on the part of one party due to one-sided contract provisions, together with terms that are so oppressive that no reasonable person would make them and no fair and honest person would accept them.”

In determining whether a contract term is unconscionable, courts will consider a variety of five major factors: (1) the bargaining positions of the parties; (2) the visibility of the clause; (3) when the contract was presented to

35. Cf. id. ("Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss.").

36. Cf. id. § 336 cmnt. b ("The amount fixed is reasonable to the extent that it approximates the actual loss that has resulted from the particular breach, even though it may not approximate the loss that might have been anticipated under other possible breaches.").

37. Cf. id. (suggesting that the anticipated or actual loss be weighed against the reasonableness of the amount of money fixed as damages in a liquidated damages clause).

38. Cf. id. ("[T]he estimate of the court or jury may not accord with the principle of compensation any more than does the advance estimate of the parties.").

39. Cf. id. ("If, on the other hand, the difficulty of the proof of loss is slight, less latitude is allowed in that approximation.").


41. Id. at 144, 739 S.E.2d at 884 (quoting Simpson v. MSA of Myrtle Beach, Inc., 373 S.C. 14, 24–25, 644 S.E.2d 663, 668 (2007)) (internal quotation marks omitted).

the other party;\(^44\) (4) the clarity of the limiting language;\(^45\) and, in some cases, (5) whether a mandatory arbitration provision combined with a limitation of liability clause is unduly burdensome.\(^46\) The burden for meeting the factors of unconscionability is high, and no single factor is determinative as to whether the provision is unconscionable.\(^47\)

The first factor focuses on the relative bargaining position of the parties, primarily looking to the sophistication of each party.\(^48\) Courts will look at the nature of the agreement and the education of the consumer to determine sophistication, along with analyzing other factors.\(^49\) When sophisticated parties agree to a contract with a limitation of liability clause in an arm’s length negotiation, a South Carolina court will almost never invalidate the limitation clause and, instead, will opt to preserve the parties’ freedom of contract.\(^50\) The courts usually reason that each of the parties possesses superior knowledge about the terms of the contract and, thus, the parties knew what they were getting themselves into.\(^51\) When businesses enter into agreements with one another, it is relatively easy to determine that the parties to the agreement were sophisticated and knew the implications of the limitation of liability clause.\(^52\) When the contract is between a consumer and a service provider, however, the meaning of sophisticated party is more difficult to ascertain.\(^53\) In Gladden v. Boykin,\(^54\) a

43. See, e.g., Gladden, 402 S.C. at 146, 739 S.E.2d at 885 (evaluating the visibility of the limitation of liability clause in a home inspection contract).
44. See, e.g., id. at 149, 739 S.E.2d at 886 (Beatty, J., dissenting) (reviewing the time at which the service providers presented the contract).
46. See, e.g., Gladden, 402 S.C. at 152-53, 739 S.E.2d at 888 (Beatty, J., dissenting) (citing Pitts v. Watkins, 905 So. 2d 553, 557-58 (Miss. 2005)) (commenting on an arbitration provision combined with a limited liability clause).
47. See id. at 145, 739 S.E.2d at 884-85 (majority opinion); id. at 150, 739 S.E.2d at 887 (Beatty, J., dissenting) (quoting Lucier v. Williams, 841 A.2d 907, 911 (N.J. Super. Ct. App. Div. 2004)).
48. See, e.g., id. at 145-46, 739 S.E.2d at 885 (reviewing the bargaining positions of the parties by analyzing their sophistication).
49. See, e.g., id. (discussing the consumer’s education level as a factor in determining whether the contract was unconscionable).
50. See, e.g., id. at 145, 146, 739 S.E.2d at 884-85 (noting that “[c]ourts should not refuse to enforce a contract on grounds of unconscionability” and upholding the limitation of liability contract).
51. See, e.g., id. at 145-46, 739 S.E.2d at 885 (indicating that both parties possessed adequate sophistication).
52. See, e.g., Georgetown Steel Corp. v. Law Eng’g Testing Co., 7 F.3d 223, 1993 WL 358770, at *3 (4th Cir. Sept. 14, 1993) (unpublished table decision) (holding that a limitation of liability clause is enforceable when parties are sophisticated business entities participating in an arm’s length negotiation).
53. Compare Gladden, 402 S.C. at 145-46, 739 S.E.2d at 885 (concluding that a consumer was a sophisticated party), with id. at 148-49, 739 S.E.2d at 886 (Beatty, J., dissenting) (concluding that the same consumer was not a sophisticated party).
54. 402 S.C. 140, 739 S.E.2d 882.
majority of the South Carolina Supreme Court stated that the parties to a home inspection contract were both sophisticated because the home inspector was a business owner and had many years of experience performing home inspections, and the home-buyer consumer was a trained real estate agent.\textsuperscript{55} The majority reasoned that the inspector and consumer were in relatively equal bargaining positions and that the consumer possessed the sophistication necessary to understand the contract to protect her own interests.\textsuperscript{56} The dissent, however, pointed out that the consumer had actually worked as a real estate agent for only a few months, several years prior, and never even had her own listings.\textsuperscript{57} The dissent argued that the fact that the consumer had “limited work in this area [was] not relevant under the circumstances” of the agreement.\textsuperscript{58} The disparity between the majority and minority view in \textit{Gladden}—regarding the sophistication of the consumer—demonstrates the difficulty in ascertaining whether a party to a contract was sophisticated enough to truly understand the terms of the agreement and their respective implications.

With respect to the second factor for determining unconscionability, the South Carolina Supreme Court recently held that “the proper test is whether an important clause was particularly inconspicuous, as if the drafter intended to obscure the term.”\textsuperscript{59} However, the inconsistency in determining the proper visibility of the clause demonstrates the difficulty in applying this factor of the test for unconscionability on a case-by-case basis. For example, in \textit{Gladden}, the majority held that the limitation of liability provision in the contract was sufficiently visible because the contract was one page long and all of the provisions were in the same size font and equally visible.\textsuperscript{60} The dissent, however, argued that because the limitation of liability clause did not stand out in the contract more than the other clauses its inconspicuousness was evidence of the clause’s unconscionability.\textsuperscript{61}

The third factor, involving the timing of contract presentation, is more straightforward to apply. The service provider must present the contract to the consumer before the service is performed, and evidence that the provider did not present the contract until after the service was performed is evidence of the unconscionable nature of the limitation of liability clause.\textsuperscript{62} In \textit{Gladden}, the dissent found it relevant that the home inspector did not present the contract to the plaintiff until after he performed the inspection.\textsuperscript{63} To the dissent, this demonstrated the plaintiff’s inability to adequately review and consent to the

\textsuperscript{55} Id. at 145–46, 730 S.E.2d at 885 (majority opinion).
\textsuperscript{56} See id.
\textsuperscript{57} Id. at 148, 739 S.E.2d at 886 (Beatty, J., dissenting).
\textsuperscript{58} Id.
\textsuperscript{59} Id. at 146, 739 S.E.2d at 885 (majority opinion).
\textsuperscript{60} Id.
\textsuperscript{61} See id. at 149, 739 S.E.2d at 886–87 (Beatty J., dissenting).
\textsuperscript{62} See, e.g., id. at 149, 739 S.E.2d at 886 (reviewing the time at which the service provider presented the home inspection contract).
\textsuperscript{63} See id.
terms of the contract, which, coupled with the inconspicuousness of the limitation of liability clause and other factors, was evidence of unconscionability. 64

The fourth factor courts consider is the clarity of the limiting language, which requires the court to construe ambiguities against the party seeking enforcement of the clause. 65 In Murray v. Texas Co., 66 the South Carolina Supreme Court held that the ambiguous language in a limitation of liability clause invalidated the clause and, therefore, deprived the drafting party of the benefit of the clause. 67 In that case, an oil company sought to enforce a limitation of liability provision in a contract with a gas station owner-operator. 68 The court reasoned that because the oil company wrote the provision into the contract, it could have easily worded the provision to limit the company’s liability in the dispute. 69 However, because the oil company failed to do so, the court construed the ambiguities in the provision against it and, therefore, did not relieve the oil company from its own negligence in performing the agreement. 70

The fifth factor applies to cases in which a contract contains both a limitation of liability clause and a mandatory arbitration clause. 71 The presence of both a mandatory arbitration clause and a limitation of liability clause in a contract is evidence of unconscionability, as the arbitration process may involve fees far in excess of any possible recovery under the limitation of liability clause. 72 The consumer is “effectively denied any recovery” because the fees are larger than the possible recovery, and “this [is] further evidence of unconscionability.” 73

Gladden v. Boykin is the South Carolina Supreme Court’s most recent decision concerning an unconscionable limitation of liability clause. The case resulted in a divided court, with Justice Beatty delivering a lengthy dissenting opinion. 74 The majority opinion raised the barrier for proving unconscionability even higher than past precedent, reasoning that “even when the substance of the terms appear grossly unreasonable,” courts should hold the limitation of liability clause unconscionable only in narrow circumstances. 75 Specifically, the clause is unconscionable—and the courts must refuse to enforce it—only when an “extreme inequality of bargaining power” exists, together with factors such as

64. See id. at 149, 153, 739 S.E.2d at 886–87, 889.
66. 172 S.C. 399, 174 S.E. 231.
67. Id. at 402–03, 174 S.E. at 232.
68. See id. at 400, 401, 174 S.E. at 231–32.
69. Id. at 402, 174 S.E. at 232.
70. Id. at 402–03, 174 S.E. at 232.
72. See id. (citing Pitts, 905 So. 2d at 557–58).
73. Id. (citing Pitts, 905 So. 2d at 557–58).
74. See id. at 146–47, 739 S.E.2d at 885.
75. Id. at 145, 739 S.E.2d at 884–85.
evidence that the drafter intended to obscure the term or that the term was unreadable.\textsuperscript{76} These factors must combine to demonstrate “that the party against whom enforcement is sought cannot be said to have consented to the contract.”\textsuperscript{77}

Unlike the majority’s narrow consideration of the inequality of bargaining power,\textsuperscript{8} the dissent made a broader inquiry into other indicators of unconscionability.\textsuperscript{79} The dissent argued that the determination of unconscionability should focus on the “fundamental fairness of the bargaining process” and the “[a]bsence of meaningful choice on the part of one party.”\textsuperscript{80} The absence of meaningful choice in asenting to the provision, under the dissent’s view, is determined by the type of injury suffered, any disproportionate bargaining power between the parties, the parties’ relative sophistication, the visibility of the term, and whether there is an “element of surprise in the inclusion of the challenged term.”\textsuperscript{81} The dissent highlighted the “importance of a case-by-case analysis” in determining unconscionability so that the courts can address the unique circumstances of each contract.\textsuperscript{82}

Additionally, in determining enforceability, courts consider whether a limitation of liability clause violates public policy, looking first to whether the contract concerns a public interest.\textsuperscript{83} Courts consider a wide variety of factors to make this determination.\textsuperscript{84} These factors include, but are not limited to, whether (1) the contracting party is a public service provider,\textsuperscript{85} (2) regulations require the contract to be filed with a state agency,\textsuperscript{86} (3) the service provider had a public duty to provide the particular service,\textsuperscript{87} (4) the contract is one for professional

\textsuperscript{76} Id. at 145, 739 S.E.2d at 885.
\textsuperscript{77} See id. at 146, 739 S.E.2d at 885.
\textsuperscript{78} See id. at 147–53, 739 S.E.2d at 885–89 (Beatty, J., dissenting) (citations omitted).
\textsuperscript{79} Id. at 148, 739 S.E.2d at 886 (quoting Simpson v. MSA of Myrtle Beach, Inc., 373 S.C. 14, 25, 644 S.E.2d 663, 669 (2007)) (internal quotation marks omitted).
\textsuperscript{80} Id. (quoting Simpson, 373 S.C. at 25, 644 S.E.2d at 669).
\textsuperscript{81} Id. (quoting Simpson, 373 S.C. at 36, 644 S.E.2d at 674).
\textsuperscript{84} See, e.g., id. at 620–21, 138 S.E.2d at 157 (“It is necessary, therefore, to first determine whether the publication . . . was in any way connected with defendant’s public service as a telephone company.”).
\textsuperscript{85} See, e.g., id. (noting that the contract was not required to be filed with the South Carolina Public Service Commission).
\textsuperscript{86} See, e.g., S.C. Elec. & Gas Co. v. Combustion Eng’g, Inc., 283 S.C. 182, 192, 322 S.E.2d 453, 459 (Ct. App. 1984) (noting that the relationship between the parties arose by private contract in its decision to uphold the validity of an exculpatory clause).
services, (5) a statute expressly allows the limitation, (6) the state has imposed statutes or regulations to protect the public interest concerned in the contract, and (7) the “public interest requires the performance of a private duty.”

If a court determines that the contract involves a public interest, the court will then look to the public policy surrounding the service the contract concerns. First, the court will look to legislative enactments to determine public policy regarding the specified service. Only if the legislation is silent regarding the nature of the contract will the court look to the “judicially crafted public policy.” The court must then make a case-by-case determination of whether the contract violates the announced public policy.

Alternatively, rather than violating a specific, announced policy, a limitation of liability clause may violate public policy for being overly broad. In Fisher v. Stevens, the South Carolina Court of Appeals recognized that when a limitation of liability clause is “so broad that it would absolve [the enforcing party] from any injury to the [other party] for any reason,” the clause is “too broad to be enforceable . . . and void as against public policy.” Although determining whether the provision in that case eliminated liability for any reason

88. See, e.g., Gladden v. Boykin, 402 S.C. 140, 155, 739 S.E.2d 882, 890 (2013) (Beatty, J., dissenting) (“The cases cited . . . do not concern professional service contracts, where different policy considerations exist because public policy is averse to allowing professional negligence to be insulated from liability by a contractual provision.”).
89. See, e.g., id. (noting that South Carolina law allows home inspection companies to limit the scope of the inspection through contract).
90. See, e.g., id. at 159, 739 S.E.2d at 891 (“Under South Carolina law, the state may impose statutory or regulatory requirements for the purpose of protecting the public interest.” (citing S.C. CODE ANN. § 40-1-10(B) (2011)).
93. Id. at 143, 739 S.E.2d at 883.
94. See id. at 144, 739 S.E.2d at 884; see also id. at 154, 739 S.E.2d at 889 (Beatty, J., dissenting) (“Expressions of public policy may be found in constitutional or statutory authority or in judicial decisions.” (citing White v. J.M. Brown Amusement Co., 360 S.C. 366, 371, 601 S.E.2d 342, 345 (2004))).
97. Id. at 297, 584 S.E.2d 149.
98. Id. at 297, 584 S.E.2d at 153 (quoting Richards, 513 N.W.2d at 121). Note that the court in Fisher used the term “exculpatory agreement” to describe the limitation of liability clause. Id. It is debatable whether this clause was a limitation of liability provision or actually an exculpatory clause. See id. at 294, 584 S.E.2d at 151; see also supra Part I.A (discussing the differentiation between limitation of liability and exculpatory clauses).
was relatively simple because of the all-encompassing language of the clause alone.\(^9\) The rule is often difficult to apply. Many times, a limitation of liability clause that does not alone absolve the enforcing party of liability will be coupled with other contractual provisions and, when read together, essentially eliminate the liability of one party to another.\(^10\) In such a scenario, the determination of whether a provision is overly broad is difficult because of the interplay of the contract provisions.

B. Limitation of Liability Clauses in Other States

Throughout the United States, courts have taken various approaches in determining the enforceability of limitation of liability clauses.\(^11\) Some state courts take the same common law-based approach as South Carolina, upholding these provisions unless they are unconscionable or violate public policy.\(^12\) Other states have a statutory scheme to address limitation of liability provisions in certain contexts.\(^13\) Additionally, some state courts use a hybrid approach and apply the state’s anti-indemnity statutes to analyze limitation of liability clauses.\(^14\) For example, an Alaska court has held that the statute prohibiting indemnification provisions in construction contracts that indemnify against a party’s sole negligence applies both to indemnity clauses and limitation of liability clauses in contracts.\(^15\) The court reasoned that because the statute states that such an indemnification clause is “void and unenforceable,” the legislature intended the statute to apply both when a party attempted to use the clause for indemnification and when a party interpreted the clause to limit liability.\(^16\) Therefore, the statute governed the limitation of liability provisions at issue in that case because the party was not seeking indemnity and the statute applied to “interpreting” the clause, as well as seeking the clause’s enforcement.\(^17\) The clause violated the anti-indemnity statute as an indemnity clause, and the party

100. See, e.g., Gladden, 402 S.C. at 152–53, 739 S.E.2d at 888 (Beatty, J., dissenting) (citing Pitts v. Watkins, 905 So. 2d 533, 557–58 (Miss. 2005)) (arguing that a limitation of liability clause paired with a mandatory arbitration provision essentially left the consumer with no adequate remedy)
101. See Gwyn, supra note 8, at 61.
103. See, e.g., VA. CODE ANN. § 54.1–411 (2013) (allowing design professionals, such as architects, to use limitation of liability provisions).
104. See, e.g., City of Dillingham v. CH2M Hill Nw., Inc., 873 P.2d 1271, 1277–78 (Alaska 1994) (holding that Alaska’s anti-indemnity statute applies to limitation of liability clauses as well). While South Carolina does have an anti-indemnity statute, South Carolina courts do not apply the statute to limitation of liability provisions. See S.C. CODE ANN. § 32-2-10 (2007).
105. See City of Dillingham, 873 P.2d at 1278.
106. See id. (quoting ALASKA STAT. § 45.45.900 (2012)).
107. See id.
seeking enforcement of the clause could not interpret the clause as a limitation of liability clause to escape the restrictions the statute placed on the enforceability of indemnity clauses. 108

While some states apply the same approach as South Carolina to limitation of liability provisions, the decisions in these states are not consistent with decisions in South Carolina, nor are the decisions consistent among other states. 109 These inconsistencies highlight the difficulty of applying the common law tests for unconscionability and public policy to determine the enforceability of limitation of liability clauses.

For example, in Lucier v. Williams, 110 the New Jersey Supreme Court held that a limitation of liability provision in a home inspection contract was unconscionable and violated New Jersey public policy. 111 Similar to Gladden v. Boykin in South Carolina, the parties entered into a home inspection contract; the defendants negligently performed the inspection; and the plaintiffs sued, alleging breach of contract and negligence. 112 The home inspector moved for partial summary judgment, claiming that the plaintiffs’ remedy was capped by the limitation of liability provision in the contract—which stated that any liability of the inspector was limited to one-half of the contract price. 113 Unlike the South Carolina court in Gladden, the Lucier court reasoned that the parties to the contract had “grossly disparate” bargaining positions and the “underlying purpose of the contract [was] worthless” because of the severely limited liability. 114 Additionally, the court reasoned that the inspector had “no meaningful incentive to act diligently in the performance of [the] home inspection” because his only potential liability was the refund of half of the inspector’s fee. 115

Thus, the South Carolina Supreme Court’s opinion in Gladden v. Boykin and the Superior Court of New Jersey’s opinion in Lucier v. Williams demonstrate the difficulty of uniformly applying the concepts of unconscionability and public

108. See id.
110. 841 A.2d 907.
111. See Lucier, 841 A.2d at 912, 916.
112. See id. at 910; see also generally Gladden v. Boykin, 402 S.C. 140, 739 S.E.2d 882 (2013) (similar facts).
113. See id.
114. Compare id. at 912, 913 (concluding that the parties had “grossly disparate” bargaining positions), with Gladden, 402 S.C. at 145–46, 739 S.E.2d at 885 (concluding that the parties had equal bargaining power).
115. Id. at 913.
policy to limitation of liability clauses in consumer contracts for services.\textsuperscript{116} While South Carolina and New Jersey examine limitation of liability clauses under the same test, the difference in outcomes highlights the difficulty in applying the “amorphous concept” of unconscionability and the interests of public policy to limitation of liability clauses in contracts.\textsuperscript{117}

IV. LIQUIDATED DAMAGES CLAUSES

Determining the enforceability of limitation of liability provisions in consumer services contracts requires a more consistent test. Fortunately, a more consistent test exists in the liquidated damages test from the Restatement (Second) of Contracts.\textsuperscript{118} South Carolina has adopted the use of the Restatement test in determining the enforceability of a challenged liquidated damages clause.\textsuperscript{119} The liquidated damages test, if applied to limitation of liability provisions, would give courts a more efficient tool to use in determining the enforceability of the provision, while accomplishing the goals of the test for unconscionability and avoiding conflicts with public policy interests. The Restatement test would allow courts to determine enforceability with more consistency.

Additionally, support for applying the liquidated damages test to limitation of liability provisions appears in the 2003 proposed amendments to Article 2 of the Uniform Commercial Code, which would have considered both unreasonably large and small amounts of liquidated damages as unenforceable penalties— unlike the current Restatement test, which considers only unreasonably large damages a penalty.\textsuperscript{120} The test, as discussed below, balances factors by looking at the parties’ intent at the time of contracting and comparing the damages agreed to with the actual damages suffered.\textsuperscript{121} If adopted with the appropriate modifications, this test would provide courts and practitioners with a consistent guide for determining the enforceability of a limitation of liability clause in a consumer services contract.\textsuperscript{122}

Although limitation of liability clauses and liquidated damages clauses are utilized for different purposes in contracts, they are comparable. The essential purpose for a limitation of liability clause is to cap liability at a certain agreed-upon amount that any damages resulting from breach of the contract cannot

\textsuperscript{116} See id. at 916; Gladden, 402 S.C. at 146, 739 S.E.2d at 885.

\textsuperscript{117} Lucier, 841 A.2d at 911 (quoting Kugler v. Romain, 279 A.2d 640, 651 (N.J. 1971)).


\textsuperscript{121} See RESTATEMENT (SECOND) OF CONTRACTS § 356 cmt. b.

\textsuperscript{122} See infra Part IV.
exceed. Similarly, liquidated damages clauses specify a certain amount to be paid by the breaching party to the nonbreaching party in the event the contract is breached. While one type of clause provides a limitation and the other a set amount of damages, the motivations for utilizing these provisions in contracts are mostly the same.

Both limitation of liability and liquidated damages clauses allow the parties to the agreement to anticipate the possible loss if the contract is breached. This predictability allows for a reduction in the cost of the services provided because the service provider can anticipate the maximum possible amount of damages it could be forced to pay if it breaches any contracts with its customers. If the service provider cannot cap liability or set it at a specific amount, the cost of services provided would increase to compensate for the potential unlimited liability in the service agreements entered into in its business. The anticipation of possible losses allows businesses and consumers to make more efficient decisions when entering into contractual agreements.

The Restatement’s liquidated damages test is a balance of two factors: (1) the actual or anticipated loss and (2) the difficulty of proof of loss. The liquidated damages provision must be a reasonable approximation of the actual loss that resulted from the particular breach or a genuine approximation of the anticipated loss at the time of contract formation.

The second factor concerns both the difficulty of proving the actual loss suffered and the difficulty in approximating the anticipated loss at the time of contract formation. The greater the difficulty in proving either the extent of the actual loss that has occurred from the breach or establishing the anticipated loss at the time of contract formation, the easier it is to show that the liquidated damages provision is a reasonable estimation of the loss under the contract.

In applying the test, courts must balance the two factors against each other. If either the actual loss or the anticipated loss at the time of contract formation is difficult to prove, courts must afford considerable latitude to the approximation of the liquidated damages. By contrast, if the difficulty in proving the loss under the second factor is slight, then courts must afford less
latitude in the approximation of the loss and require more precision in the
liquidated damages provision.\textsuperscript{135}

In other words, if the extent of the actual or anticipated loss under
the contract is uncertain and speculative, then the courts will defer to the judgment
of the parties at the time of contracting.\textsuperscript{136} If, however, the extent of actual or
anticipated loss is relatively easy to determine, then the courts will afford less
deferece to the judgment of the parties at the time of contracting and compare
the liquidated damages to the actual loss suffered.\textsuperscript{137} The liquidated damages
provision is unenforceable as a penalty if the actual loss suffered is much less
than the amount of damages provided for in the liquidated damages provision.\textsuperscript{138}
The provision is only unenforceable if it is a penalty—if it causes the breaching
party to pay much more than the actual loss suffered by the nonbreaching
party.\textsuperscript{139} The provision is enforceable if it is reasonable under the balancing test,
even if the provision provides for much less recovery than the actual losses
suffered.\textsuperscript{140}

South Carolina courts apply the test set out in the Restatement with some
inconsequential modifications.\textsuperscript{141} Courts apply the Restatement test as follows:
“[W]hether the sum stipulated in the [contract] is a liquidated damage or an
unenforceable penalty is whether the amount is reasonably intended by the
parties as the predetermined measure of compensation for actual damages that
might be sustained by reason of nonperformance.”\textsuperscript{142} Courts consider factors
such as “[the contract’s] subject matter, the ease or difficulty in measuring the
breach in damages and the magnitude of the stipulated sum, not only as
compared with the value of the subject of the contract, but in proportion to the
probable consequences of the breach.”\textsuperscript{143}

In \textit{Erie Insurance Co. v. Winter Construction Co.},\textsuperscript{144} the South Carolina
Court of Appeals applied the Restatement test to uphold a liquidated damages
provision in a construction contract that provided for a percentage of the
outstanding contract amount to be paid in the event of breach.\textsuperscript{145} Because of the
impossibility of determining the anticipated damages in the event of a breach and
the difficulty in proving the actual damages resulting from the breach, the court

\textsuperscript{135} See id.
\textsuperscript{136} See id.
\textsuperscript{137} See id.
\textsuperscript{138} Id. \S 356(2), \S 356 cmt. b.
\textsuperscript{139} See id.
\textsuperscript{140} Id. \S 356 cmt. b.
\textsuperscript{141} See, e.g., Erie Ins. Co. v. Winter Const. Co., 393 S.C. 455, 462, 713 S.E.2d 318, 322 (Ct. App. 2011) (noting that the touchstone question for distinguishing a liquidated damages clause from an unenforceable penalty is a test based on the Restatement (quoting Tate v. Le Master, 231 S.C. 429, 441, 99 S.E.2d 39, 45–46 (1957))).
\textsuperscript{142} Id. (quoting Tate, at 441, 99 S.E.2d at 45–46) (internal quotation marks omitted).
\textsuperscript{143} Id. (quoting Foster v. Roach, 119 S.C. 102, 107, 111 S.E. 897, 899 (1922)).
\textsuperscript{144} 393 S.C. 455, 713 S.E.2d 318.
\textsuperscript{145} Id. at 458, 465, 713 S.E.2d at 319–20, 323.
reasoned that the percentage formula used in the liquidated damages provision was fair and reasonable.\(^\text{146}\)

Alternatively, a liquidated damages provision in a contract is unenforceable if the court determines that the provision is actually a penalty, rather than a genuine anticipation of damages.\(^\text{147}\) In *Foreign Academic & Cultural Exchange Services, Inc. v. Tripon*,\(^\text{148}\) the South Carolina Supreme Court held that the liquidated damages provision in a teacher’s employment contract for a foreign exchange teaching program was an unenforceable penalty.\(^\text{149}\) The liquidated damages provision provided that the teacher was obligated to pay a sum not less than $36,000 in the event of her breach, which would allegedly represent the amount of the company’s lost investment in the teacher.\(^\text{150}\) The company sued, arguing that the teacher’s failure to return to her home country violated the terms of the agreement and required her to pay the stipulated amount.\(^\text{151}\) The court, however, reasoned that the stipulated sum was an unenforceable penalty because the stipulated amount was “plainly disproportionate to any probable damage[s] resulting from respondent’s failure to return home,” and the lost investment amount claimed by the company was a sunk cost on which the teacher’s failure to return home had no effect.\(^\text{152}\) The provided-for damages had no relationship to the actual damages the company might sustain; thus, the provision was an unenforceable penalty.\(^\text{153}\) The court balanced the actual damages suffered with the prospective loss at the time of contracting and determined that, because the actual damages suffered were so low compared to the provided-for damages, the provision was an unenforceable penalty—even if the damages were difficult to approximate at the time of contract formation.\(^\text{154}\)

The shortcoming of the liquidated damages test from the Restatement is that a liquidated damages provision is unenforceable only if the sum stipulated is too high compared to the actual damages suffered and is, thus, a penalty on the party paying damages.\(^\text{155}\) This one-sided view of a penalty raises the question of what happens when the liquidated damages provision is too low in comparison to the actual damages suffered. The Restatement expressly provides that the liquidated damages test does not contemplate provisions that fix damages in an unreasonably small amount, but instead suggests that unreasonably small

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146. See *id.* at 463, 713 S.E.2d at 322.
149. *Id.* at 201, 204–05, 715 S.E.2d at 333, 334.
150. *Id.* at 201, 204, 715 S.E.2d at 333, 334.
151. *Id.* at 201, 715 S.E.2d at 333.
152. *Id.* at 204, 715 S.E.2d at 334.
153. *Id.* at 204–05, 715 S.E.2d at 334.
154. *Id.*
amounts may be considered unconscionable under another section of the Restatement.\textsuperscript{156}

However, fixing damages in an unreasonably small amount can be just as penalizing as fixing damages in an unreasonably large amount. If damages are provided in an unreasonably small amount compared to the actual loss, the penalty is on the nonbreaching party, who is left without an adequate remedy—while the breaching party walks away from the failed agreement much better off. A logical analysis would treat both unreasonably large and unreasonably small liquidated damages as penalties and, thus, as unenforceable.

V. A NEW TEST FOR LIMITATION OF LIABILITY CLAUSES

Fixing the shortcoming in the liquidated damages test in the Restatement provides a test to remedy the burdensome and inconsistent application of South Carolina courts’ current analysis of limitation of liability clauses. The test’s exclusion of liquidated damages provisions that set damages at an unreasonably low amount demonstrates these provisions are not considered penalties.\textsuperscript{157} Yet, the Restatement provides that a liquidated damages provision that sets damages in an unreasonably low amount “may be unenforceable as unconscionable.”\textsuperscript{158}

Thus, a liquidated damages provision that is unreasonably low could be considered a penalty in one sense because of the potential limited recovery available.\textsuperscript{159} A liquidated damages provision setting the amount of recovery in an unreasonably low amount is comparable to a limitation of liability provision. However, the liquidated damages section of the Restatement “does not purport to cover the wide variety” of damage limiting provisions that exist in contracts.\textsuperscript{160}

While the Restatement does not apply the liquidated damages section to unreasonably low damages,\textsuperscript{161} a court could logically apply the liquidated damages test to limitation of liability clauses that unreasonably limit the remedy available for breach of a contract. A limitation of liability provision that unreasonably limits damages is essentially a liquidated damages provision that is unreasonably low because both clauses provide for an unreasonably low amount of recovery for contract breach.

Using a test comparable to the liquidated damages test to determine enforceability of a limitation of liability provision would avoid the burdensome considerations of public policy and unconscionability, while accomplishing the same goals that these inquiries are meant to accomplish. The test would also allow contracting parties to assess whether the clause reasonably estimates the possible damages and, therefore, will be enforceable—rather than facing

\textsuperscript{156} Id. § 356 cmt. d (referring to § 208).
\textsuperscript{157} See id.
\textsuperscript{158} Id. § 356 cmt. a (emphasis added).
\textsuperscript{159} See id. § 356 cmt. d.
\textsuperscript{160} Id.
\textsuperscript{161} See id.
uncertainty over whether the clause will get thrown out on the grounds of public policy, unconscionability, or both. 162

Specifically, South Carolina courts should adopt a test that examines whether the limitation of liability provision was a reasonable allocation of the potential damages at the time of contracting. First, the courts should compare the actual damages suffered as a result of the breach to the estimate of damages in the limitation of liability provision. If at the time of contracting the damages are relatively easy to estimate, the courts should require more precision in estimating the limitation of damages. If, however, at the time of contracting the potential damages are not capable of reasonable estimation, then courts should require less precision in the limitation of liability compared to the actual harm suffered. If the actual damages suffered are not capable of assessment, then the focus should be on the intention of the parties at the time of contracting and whether the limitation of liability was a reasonable estimation of the potential damages under the agreement.

Applying the liquidated damages test to a limitation of liability clause simplifies the inquiry into whether the clause is enforceable, while ensuring that the clause is not unconscionable and does not conflict with public policy. 163 Inherent in the concepts of unconscionability and public policy are the ideas of fairness of the bargain and a reasonable remedy for breach of the agreement. 164 Looking to the intent of the parties at the time of contracting, as well as the difficulty in estimating damages, accomplishes the underlying goals of public policy and unconscionability. 165 Parties cannot genuinely allocate the possible loss if the remedy provided in the contract is grossly unfair to one party. 166 Additionally, the test preserves the parties’ interest in freedom of contract. If the parties’ intent at the time of contracting is to limit the remedy, the desires of the parties will be upheld as reasonable under the circumstances because the parties intended the limitation.

The relevant public policy interests are also preserved under this test. 167 Comparing the limitation of liability to the actual damages suffered prevents contracts from unfairly favoring service providers over consumers. A service provider cannot insert a clause in a contract that leaves the consumer with only nominal recovery because the service provider must make a reasonable allocation of the risk when drafting the agreement. Thus, a service provider

162. The public policy and unconscionability considerations would still apply to limitation of liability clauses, but the test would be used as a means to meet the goals of these policies without the difficult analysis of the respective policies.
164. See id. at 147–54, 739 S.E.2d at 885–90 (Beatty, J., dissenting) (citations omitted).
165. See supra notes 40–82 and accompanying text.
166. See supra note 41 and accompanying text.
167. See supra notes 83–100 and accompanying text.
cannot limit the consumer’s remedy below an amount it knows is a reasonable possible loss in the event of breach.

In the context of a home inspection contract, applying the liquidated damages test to the limitation of liability clause would ensure that the homeowner is not left without a remedy.\(^{168}\) The liquidated damages test would render the limitation of liability clause unenforceable if the remedy the consumer is left with after the breach of contract is simply the return of the inspection fee. At the time of contracting, the estimate of loss to either party resulting from a breach of the contract would have to be made, and the return of the inspection fee usually is not an adequate remedy. Even though the potential damages are not capable of precise estimation, limiting the damages to the inspection fee is unreasonably low. The actual damages that could result from a faulty inspection could be grossly disproportionate when compared to the inspection fee itself. In this situation, the limitation of liability clause should be stricken as unenforceable. Striking limitation of liability clauses that cap the damages at a return of the inspection fee gives service providers an incentive to arrive at a reasonable estimate of prospective loss in the limitation of liability clause.

The proposed balancing test provides protection for consumers and preserves the parties’ interest in freedom of contract. The intention of the test is to reach a middle ground between unreasonably limited remedies in contracts due to overly restrictive limitation of liability clauses and allowing for businesses to protect against unlimited liability in the interest of providing the best service at the cheapest price. The test accomplishes these goals by focusing on reasonableness under the circumstances of the contract and the intent of the parties to the contract.\(^{169}\) While this test may not have a flawless application to the competing interests of the consumer and the service provider, it allows for the efficient determination of the enforceability of a limitation of liability clause when adverse interests are involved in a breach of contract action.

VI. CONCLUSION

The tests for unconscionability and public policy considerations currently employed by South Carolina courts to determine the enforceability of limitation of liability clauses in consumer contracts for services are inconsistently applied and favor service providers.\(^{170}\) If South Carolina applied the balancing test from the Restatement to limitation of liability clauses, the same goals of the current


\(^{169}\) Cf. supra notes 33–39 and accompanying text (discussing the Restatement test for determining the enforceability of liquidated damages clauses).

\(^{170}\) Compare Gladden, 402 S.C. at 146, 739 S.E.2d at 885, with Simpson v. MSA of Myrtle Beach, Inc., 373 S.C. 14, 34, 644 S.E.2d 663, 674 (2007), and Gladden, 402 S.C. at 147, 739 S.E.2d at 885 (Beatty, J., dissenting) (demonstrating the inconsistent application of the current tests).
tests would be accomplished in a more consistent and efficient manner. Additionally, consumers would be better protected from overly burdensome limitations on liability by the reasonableness requirement of the liquidated damages balancing test.

*S. Harrison Williams*