CONTRACTS LIMITING LIABILITY: A PARADOX WITH TACIT SOLUTIONS

BLAKE D. MORANT*

I. INTRODUCTION ................................................................................................................. 716
II. THE “TRADITIONAL MODEL:” PRESENT RULES THAT GOVERN THE ENFORCEABILITY OF CONTRACTS LIMITING LIABILITY .......................................................................................................................... 729
   A. Restrictions Predicated Upon the Concept of “Public Policy” ........................................ 734
   B. Public Policy: Paternalistic Considerations Rooted in Concepts Related to Unconscionability ................................................................. 735
   C. Public Policy: Paternalistic Considerations Related to the Protection of Third Parties ........... 737
   D. Public Policy: Paternalistic Considerations Related to the Concept of Public Duty and Operation of Law ..... 740
   E. Manifestation of Paternalism: Strict Construction of Contracts Limiting Liability .................. 743
   F. Paternalistic Considerations Relevant to Indemnity Agreements Among Common Carriers ............... 745
III. CONTRACTS LIMITING LIABILITY: EVALUATING PUBLIC POLICY RATIONALE ......................................................................................................................... 750
   A. Contracts Limiting Liability Among Common Carriers: Prejudicial Factors of Public Policy ............ 752
      1. Bargainers’ Motivation to Contract: Risk Aversion ......................................................... 752
      2. Prejudicial Factors: Bargaining Power Disparity .............................................................. 754

* Associate Professor of Law, The University of Toledo College of Law. J.D., B.A., University of Virginia. Former Assistant General Counsel, Washington Metropolitan Area Transit Authority, 1987-92. I sincerely thank the following individuals without whom this project could not have been completed: Professors Lawrence Ponoroff, Daniel Steinbock, Marshall Leaffer, and Geraldine Moohr, whose reviews of earlier drafts contributed significantly to the piece; Douglas Waymire, my diligent research assistant; Mrs. Peggie Cummings, my secretary; and Paulette J. Morant, my very supportive wife. I also acknowledge the funding support provided by the University of Toledo College of Law Summer Research Grant.
I. INTRODUCTION

The concept of “freedom” or “liberty” maintains significant roots within the lexicon of contract law.1 “Freedom of contract”2 signifies that parties to an agreement have the right and power to construct their own bargains.3 The Supreme Court’s landmark

---

1. See Samuel Williston, Freedom of Contract, 6 CORNELL L.Q. 365, 366 (1921) (noting that the concept of “freedom” constitutes a definitive base of the Declaration of Independence and reflects Jeffersonian democracy, thereby facilitating individual action and minimizing governmental activity or interference).

2. For the purposes of this Article, the terms “freedom” and “liberty” comprise synonymous terms; therefore, the phrases “freedom of contract” and “liberty of contract” share the same connotation.

3. See Brokers Title Co. v. St. Paul Fire & Marine Ins. Co., 610 F.2d 1174, 1178-79 (3d Cir. 1979); see also Duncan Kennedy, Distributive and Paternalist Motives in Contract and Tort Law, with Special Reference to Compulsory Terms and Unequal Bargaining Power, 41 Md. L. Rev. 563, 570 (1982). Professor Kennedy indicates that the notion of freedom of contract fits within the “domain of pre-existing property rights.” Id. at 568. Irrespective of the traditional notion of freedom of contract that entails an individual’s freedom to make, or not to make, agreements, Professor Kennedy recognizes that fostering of the freedom of contract notion by decision makers embodies the power not only to enforce agreements but also to refuse enforcement of agreements. Id. at 569. This balance of non-intervention and over-intervention, which are freedoms, serves to justify the imposition of paternalistic rules regarding the refusal to enforce certain agreements that are contrary to the interests of one of the bargainers. Id. at 569-70.
opinion in *Lochner v. New York* recognizes the significance of private autonomy and efficiency in the formulation of specific bargains.\(^4\) Indeed, the notion of "freedom of contract" constitutes a historical concept with philosophical origins.\(^5\) Strict adherence to this ideology would require courts to honor parties' bargains and refrain from tampering with the terms thereof.\(^6\) Some theorists who believe strongly in the notion opine that laws "interfer[ing] with private arrangements" should be invalidated.\(^7\) Irrespective of philosophical differences regarding the extent of adherence to the notion of freedom of contract, the concept may suffer from definitional ambiguities.\(^8\) Critics have noted that the concept lacks sufficient clarity and definiteness.\(^9\)

---

4. 198 U.S. 45, 52-65 (1905).
8. The term "freedom" has a variable definition that may have different connotations to different individuals. See Williston, *supra* note 1, at 366 (noting that "[w]ords acquire curious connotations in the course of time").
9. Some theorists note that freedom of contract tends to be incoherent since the notion rests upon the concept of voluntariness, which can be elastic. See Note, *supra* note 6, at 978 (explaining that "contract law has been bereft of an uncontroversial guiding norm since the realists exposed the incoherence of the idea of 'freedom of contract' in the 1930's"). Specifically, "the realists showed that freedom of contract was incoherent because it depended on the elastic concept of 'voluntariness.' They demonstrated that choosing which agreements were voluntary and thus enforceable required controversial policy decisions about the application of state force." *Id.* at 978 n.5; Betty Mench, *Freedom of Contract as Ideology*, 33 STAN. L. REV. 753, 755 (1981) (noting that the "principle of free contract is incoherent on its own terms" (emphasis omitted)) (book review). Elasticity of voluntariness can promote ambiguity in freedom of contract without also providing an appropriate remedy. *See generally* Note, *supra* note 6 (comparing the "Chicago" and
Although debate regarding adherence to the doctrine continues, modern views of freedom of contract recognize that the concept of "freedom" has limitations. The Supreme Court no longer appears to consider "freedom of contract" a constitutional absolute, at least within the context of labor law. Moreover, the state may legitimately restrict the parties' right to contract if the proposed bargain is found to have some deleterious effect on the public or to contravene some other matter of public policy. Contracts that limit the negligence of others tend to attract such scrutiny.

"liberal" models of economic analysis of contract law and concluding that both fail to provide a noncontroversial method of decision making). Additional confusion regarding the freedom of contract notion involves the extent to which parties may define their actions with respect to the bargain entered. It may be theorized that parties are free to enter into an agreement, but that their rights and duties pursuant to such an agreement may be fixed independent of the bargain reached by the parties. See Williston, supra note 1, at 379.

10. A number of theorists advocate greater emphasis upon and adherence to the strict notion of freedom of contract. See Butler & Ribstein, supra note 7, at 808; Conant, supra note 7, at 789-90; Epstein, supra note 7, at 705.

11. Limitations on freedom of contract may involve questions of degree, depending upon the time, place, and circumstances relevant to such limitations. Williston, supra note 1, at 379. States may also have "reserved power under the contract clause" to interfere with contracts if such action is deemed necessary to promote a public interest. Butler & Ribstein, supra note 7, at 781.


13. Contracts that contravene social policies, as articulated by legislators, may be found void even though common law may allow their enforcement. See Cathleen M. Devlin, Comment, Indemnity and Exculpation: Circle of Confusion in the Courts, 33 Emory L.J. 135, 135 n.1 (1984). Police powers are permissible to promote "'safety, health, morals, and the general welfare of the public.'" Williston, supra note 1, at 375-76 (quoting Lochner v. New York, 198 U.S. 45, 53 (1905)). Limitations under a state's police powers on the freedom of contract are permissible unless such limitations are deemed to be arbitrary and capricious. Id. at 378.


We have had frequent occasion to consider the limitations on liberty of contract. While it is highly important to preserve that liberty from arbitrary and capricious interference, it is also necessary to prevent its abuse, as otherwise it could be used to override all public interests and thus in the end destroy the very freedom of opportunity which it is designed to safeguard.

We have repeatedly said that liberty of contract is a qualified and not an absolute right.

Id.; see infra part II.C.
This Article proposes that the law governing contracts that limit liability, and perhaps all voluntary transactions, should employ a more accurate, uniform, and balanced methodology to evaluate the enforceability of such agreements. The present framework explicitly tends to emphasize public policy concerns related to paternalism. This emphasis should be clarified and expanded to include an evaluation of the possible benefits provided by such agreements.

Public policy concerns, which presently focus on paternalistic goals, should not be narrowly construed so as to thwart potential agreements that maximize the utility of scarce resources and promote overall efficiency. Public policy considerations must encompass the evaluation of the societal benefit provided by the parties' agreement. The inclusion of these

15. Research of this topic revealed an interesting and compelling point regarding credibility. Ellen Smith Pryor, noting the persuasiveness of Susan Estrich's article on rape, emphasized the importance of an author's experiences relevant to the subject matter on which he or she writes. See Ellen S. Pryor, The Tort Law Debate, Efficiency, and the Kingdom of the II: A Critique of the Insurance Theory of Compensation, 79 VA. L. REV. 91, 94 n.11 (1993) (quoting Susan Estrich, Rape, 95 YALE L.J. 1087, 1089 (1986), who said that she "[could] not imagine anyone writing an article on prosecutorial discretion without disclosing that he or she had been a prosecutor"). Commensurate with this thought, I should elucidate some of my experiences that compelled me to write on the topic of contracts limiting liability.

For five years, I served as Assistant General Counsel with the Washington Metropolitan Area Transit Authority (Authority). In that capacity, I had the opportunity to review, and give advice upon agreements that the Authority had entered into with established rail carriers that own tracks and property on which the Authority operated its light rail transit system. These agreements with the established carriers include clauses requiring the Authority to indemnify the established carrier in the event of an accident. See Booz, Allen & Hamilton, Inc., WMATA Common Corridor Study: Final Report 2-8 (1989) [hereinafter WMATA Common Corridor Study]. Notwithstanding the execution of these agreements many years prior to my review, the problems relevant to the enforceability of these clauses remained at issue and continued to generate vigorous debate. While no incident occurred to trigger the implementation of the liability clause of the agreement, the omnipresent question remains whether the Authority will be strictly bound by the terms of its indemnity clause in light of considerations of public policy.

16. Paternalism, which manifests empathy or love, "involves compelling a decision [which generally is not in accord with the original bargain] on the ground that it is in the beneficiary's best interest." Kennedy, supra note 3, at 625. Consequently, decision makers alter the original bargain when paternalistic concerns dictate that the bargain is somewhat flawed. Id. at 624-25.

17. Paternalistic intervention seeks as its main object the protection of one of the parties to the agreement. Id. at 624. Any distributive effects of such paternalistic actions tend to be side effects rather than the true purpose of such intervention. Id. at 625.

18. See infra text accompanying notes 222-233.
positive, and perhaps implicit, factors that relate to the concept of "public policy" may already constitute an inherent element in the evaluation of indemnity agreements between common carriers.\textsuperscript{19} These notable positive benefits, together with the minimization of certain negative concerns that focus on paternalism,\textsuperscript{20} contribute to the validity and enforceability of indemnity agreements between common carriers. Consequently, the benefits of positive attributes should be explicitly incorporated in the evaluation of all contracts that seek to limit liability, and moreover, in voluntary transactions generally. Subsumption of this evaluative factor in the decision-making process should lead to more consistent enforcement of such bargains and afford greater certainty to parties that their original bargains and concomitant expectations will be maintained, thereby causing the economy to operate smoothly.\textsuperscript{21}

Part II of this Article presents the conventional model that currently governs the enforceability of contracts limiting liability. This section delineates the present policies relevant to such bargains.\textsuperscript{22} Concerns relevant to contracts that limit liability include policy considerations that tend to restrict the enforceability of these agreements. This Article then specifically elucidates the law governing indemnity agreements between common carriers. While public policy considerations concerning adherence to public

\textsuperscript{19} Indemnity agreements between common carriers appear to contain definite societal benefits. Arguably, these residual benefits, while not explicitly acknowledged, may be a consideration in the evaluation of the enforceability of such agreements. \textit{See infra} note 201 and accompanying text.

\textsuperscript{20} \textit{See infra} part II.F.

\textsuperscript{21} Kennedy, \textit{supra} note 3, at 566-70.

\textsuperscript{22} There are relatively few comprehensive and timely pieces that examine contracts limiting liability with respect to the constraints and implications related to the theory of contract law. \textit{See generally} Scott Conley & George Sayre, \textit{Rights of Indemnity As They Affect Liability Insurance}, 13 HASTINGS L.J. 214 (1961) (discussing the rights of indemnity between two defendants or their insurers under California law); E. Eugene Davis, \textit{Indemnity Between Negligent Tortfeasors: A Proposed Rationale}, 37 IOWA L. REV. 517 (1952) (examining the issue of indemnity when there are no express contracts to indemnify); Harold A. Meriam Jr. & John V. Thornton, \textit{Indemnity Between Tort-Feasors: An Evolving Doctrine in the New York Court of Appeals}, 25 N.Y.U. L. REV. 845 (1950) (reviewing the history of New York law of indemnity of tortfeasors, particularly as it relates to instances of complete indemnification); Lawrence Potamkin & Norman L. Plotka, \textit{Indemnification Against Tort Liability—The "Hold Harmless" Clause—Its Interpretation and Effect Upon Insurance}, 92 U. PA. L. REV. 347 (1944) (discussing the interpretative difficulties inherent in bilateral and unilateral hold harmless clauses); James B. Smith, \textit{Contractual Controls of Damages in Commercial Transactions}, 12 HASTINGS L.J. 122 (1960) (examining the issue of whether the enforcement of liquidated damages clauses would result in a forfeiture).
duty contribute to the skepticism of indemnity agreements in general, such agreements between common carriers tend to have an enhanced probability of enforcement given the characteristics of the parties and the nature of their bargains.

Part III of this Article analyzes the present law governing contracts limiting liability, closely scrutinizing the public policy factors that fuel concern for paternalism. The present model's preoccupation with paternalism actually focuses on negative factors that have been explicitly articulated as a basis for limiting such agreements. In addition to an analysis of the traditional public policy considerations governing indemnity agreements, Part III continues with an examination of policy considerations relevant to indemnity agreements among common carriers. Notwithstanding the negative factors inherent in the explicit concern for paternalism, the seeming tolerance for such agreements among common carriers primarily must be due to a tacit consideration of the residual benefits of these agreements. These benefits or positive factors can often include the probability that the agreement will foster the efficient, and perhaps optimal, use of existing scarce resources.

Ultimately, the decision of whether to enforce contracts limiting liability should include the weighing of both negative and positive factors inherent in such agreements. If negative factors are diminished or alleviated by externalities, i.e., statutory or regulatory control or self-interest of the bargainers, and discernible positive factors truly exist, then agreements imbued with such qualities warrant enforcement. This modification of the traditional model would lead to a more efficacious mechanism for evaluating not only contracts limiting liability, but also other types of voluntary transactions.

Restrictions and caveats placed upon contracts limiting negligence liability contribute to the illusory nature of the freedom of contract notion. The following hypothetical situation serves as illustration. X, a small business involved in the production and

23. See infra text accompanying notes 164-165.
24. Common carriers include a variety of entities. See infra note 130. The analysis in this Article will focus on the railroad industry, subway, and light rail operators and suggest that the arguments deduced from the analysis of the railroad industry should be applicable to other common carriers.
sale of homemade widgets, enters into an agreement with Y, an adjacent small business owner, for the use of Y’s land to transport X’s goods. X seeks to obtain a right-of-way upon a small portion of Y’s property to facilitate transportation of its goods. Y charges X a fee for the use of her property and insists that X indemnify and hold Y harmless for any damages or liabilities resulting from X’s or Y’s negligence. X seeks the agreement with Y as a less expensive alternative that accommodates the transportation of X’s goods.\(^{25}\) Y receives not only compensation for the use of her property, but also coverage against any liability exposure incident to X’s use of the property. The agreement provides X with a less expensive alternative for the transportation of its goods and, in all probability, lower market prices and increased accessibility for such goods. The arrangement between X and Y, which represents a contract designed to limit liability, constitutes a hold harmless\(^{26}\) or indemnity\(^{27}\) agreement.\(^{28}\)

Despite X and Y’s good faith efforts\(^{29}\) to enter into a bargain that is mutually beneficial to both parties concerning the use of resources and economic interests, the viability of their agreement remains speculative due to anxieties rooted in public policy.\(^{30}\)

\(^{25}\) Note that X’s alternatives include a more circuitous route to transport its goods or the purchase of that portion of Y’s property necessary for the transportation of the goods. Both alternatives are significantly more expensive than the right-of-way agreement with Y.

\(^{26}\) “Hold harmless” agreements have been defined as “contractual arrangement[s] whereby one party assumes the liability inherent in a situation, thereby relieving the other party of responsibility” or as “[a]greement[s] or contract[s] in which one party agrees to hold the other without responsibility for damage or other liability arising out of the transaction involved.” Dresser Indus. v. Page Petroleum, Inc., 853 S.W.2d 505, 508 (Tex. 1993) (quoting BLACK’S LAW DICTIONARY 658 (5th ed. 1979)); see also New York C.R.R. v. General Motors Corp., 182 F. Supp. 273, 291 (N.D. Ohio 1960).

\(^{27}\) “Indemnity” has been defined as “the obligation resting on one party to make good a loss or damage another party has incurred.” Agricultural Sers. Ass’n v. Ferry-Morse Seed Co., 551 F.2d 1057, 1072 (6th Cir. 1977) (quoting Rossmoor Sanitation, Inc. v. Pylon, Inc., 532 P.2d 97, 100 (Cal. Ct. App. 1975)); see also Brown v. Seaboard Coast Line R.R., 554 F.2d 1299, 1304 n.5 (5th Cir. 1977) (defining “indemnity” to mean “reimbursement, restitution, or compensation” (quoting Parker v. Puckett, 199 S.E.2d 343, 346 (Ga. Ct. App. 1973)).

\(^{28}\) Indemnity and hold harmless agreements constitute types of contracts that limit liability. Throughout this Article, I will refer to all such agreements as either “contracts limiting liability” or “indemnity agreements.” Differences in nomenclature do not alter the analysis.

\(^{29}\) See infra notes 180-181 and accompanying text for a discussion of good faith dealing.

\(^{30}\) See infra part II.A.
judiciary generally views indemnity agreements, such as the one adopted by X and Y, with a degree of skepticism and suspicion.\textsuperscript{31} Although the more modern rule dictates that the agreement between X and Y may be enforceable,\textsuperscript{32} public policy constraints,\textsuperscript{33} notwithstanding legislative proscriptions in many jurisdictions,\textsuperscript{34} potentially limit these agreements.\textsuperscript{35} Regardless of the parties' informed intent to formulate such a bargain, agreements between private parties such as X and Y remain vulnerable to either strict judicial scrutiny at the very least,\textsuperscript{36} or a complete invalidation at the extreme.\textsuperscript{37}

This skepticism of indemnity agreements basically reflects a paternalistic concern for both X, an individual who may feel compelled to accept such an agreement, and the public, which may unsuspectingly experience negative effects of that agreement. These paternalistic concerns include a need to protect X, the indemnitee, who entered the agreement from a perceived disadvantageous bargaining position.\textsuperscript{38} The other element of paternalism focuses on the protection of third parties due to the

\textsuperscript{31} See infra notes 83-86 and accompanying text.
\textsuperscript{32} Contracts limiting the liability of the originating party tend to be sustainable; however, contracts whereby a party indemnifies the negligent acts of another party were historically disfavored. See Kansas City Power & Light Co. v. United Tel. Co., 458 F.2d 177, 179 (10th Cir. 1972) (recognizing the general rule "that private contracts exculpating one from the consequences of his own acts are looked upon with disfavor by the courts"); McDowell v. Canron Corp., 710 P.2d 192, 195 (Wash. 1985) (en banc) (stating that "[d]ecisions of this court support ... disfavor of contracts to indemnify a party against losses caused by its own negligence"). While the modern rule allows for agreements whereby party X assumes responsibility for the negligence of party Y, such agreements are extensively scrutinized and subject to limitation due to public policy concerns and enactments by legislatures. See Linkowski v. General Tire Co., 371 N.E.2d 553, 554, 556 (Ohio Ct. App. 1977) (citing state legislation voicing Ohio's public policy against construction contractors indemnifying themselves against their own negligence); Dayton Fabricated Steel Co. v. Dayton Town & Country, Inc., 133 N.E.2d 423, 425 (Ohio Ct. App. 1954) (agreeing that indemnity clauses shielding a defendant from the consequences of his own negligence call for "careful scrutiny"); Devlin, supra note 13, at 138 (explaining that "[w]hile indemnity and exculpatory clauses are generally enforceable, courts have struck these clauses down" because they "might contradict the public policy intent effectuated by a statute"). For further explanation and details concerning such agreements, see infra part II.
\textsuperscript{33} See infra part II.A-D.
\textsuperscript{34} See infra note 120.
\textsuperscript{35} See infra notes 121-122 and accompanying text.
\textsuperscript{36} See infra notes 125-129 and accompanying text.
\textsuperscript{37} See infra notes 130-138 and accompanying text.
\textsuperscript{38} See infra notes 171-173 and accompanying text for a discussion on "unequal bargaining position" as it relates to the broad concept of unconscionability.
agreement’s possible facilitation of reckless conduct by Y, the indemnitee.\footnote{See infra text accompanying notes 184-188.}

Courts desire neither to encourage antisocial conduct on the part of individuals such as Y who enjoy coverage under the agreement, nor to give judicial approval of such action.\footnote{See RESTATEMENT (SECOND) OF CONTRACTS ch. 8, Introductory Note, at 2-4 (1981) [hereinafter CONTRACTS].} In the hypothetical transaction of X and Y, public policy concerns focus on the agreement’s impact upon the public service duties of Y or the possible violation of a statutory duty required of Y.\footnote{E.g., Kuhn v. State, 692 P.2d 261, 263-65 (Alaska 1984); see infra part II.D. The Kuhn court noted that an indemnity provision invites judicial skepticism when it tends “to promote breach of a duty owing to the public at large” or when it encourages the violation of a statutorily-created duty. Kuhn, 692 P.2d at 263 (quoting Manson-Osberg Co. v. State, 552 P.2d 654, 659-60 (Alaska 1976)). The court cited two policy justifications for this position. First, public servants “must be required to guard against the consequences of [their] negligence.” Id. at 266. Second, “it may be unfair to allow [public servants] to impose ‘liability-avoiding agreements on those [they are] supposed to serve, since the latter have no choice but to accept such agreements.’” Id. (quoting Burgess Constr. v. State, 614 P.2d 1380, 1382 (Alaska 1980)); see Smith v. Seaboard Coast Line R.R., 639 F.2d 1235, 1239 (5th Cir. Unit B Mar. 1981) (noting that indemnity contracts are generally valid when they are “expressed in clear and unequivocal terms, . . . except when such an agreement is prohibited by statute or where a public duty is owed”); Titan Steel Corp. v. Rust Eng’g Co., 365 F.2d 542, 548 (10th Cir. 1966) (expressing the federal view that indemnity agreements may violate public policy, “especially contracts affected with a public interest and involving the performance of a public duty”); Batson-Cook Co. v. Georgia Marble Setting Co., 144 S.E.2d 547, 549 (Ga. Ct. App. 1965) (recognizing that “[e]xcept in cases prohibited by statute, or where a public duty is owed,” indemnity contracts are valid and are “not void as against public policy”).} Consequently, the restrictions placed upon indemnity agreements remain rooted in the public obligation to protect third parties from possible reckless conduct on the part of indemnitees.\footnote{See infra notes 184-188 and accompanying text.}

Curiously, not all contracts that limit negligence liability share as dubious a fate as the agreement between X and Y. For example, A, a United States municipality, seeks to spur commerce in its inner-city business district. A also would like to alleviate its burgeoning traffic and parking problems and reduce air pollution. In an effort to achieve these goals, A decides to establish a light rail commuter service, such as a trolley or a subway, that would extend into neighboring suburbs. One goal of A’s project would be to encourage individuals to rely less on privately owned vehicles that contribute to traffic congestion and air pollution. A also intends to
provide a safe, economical, and efficient mode of transportation into the city.

A seeks to construct and operate its light rail system in the most efficient and least expensive manner available. Notwithstanding these goals, construction of light rail facilities, which include passenger stations and rail tracks extending into the suburbs, may lead to exorbitant acquisition costs. A's planners observe that B, a large regional freight railroad conglomerate, has tracks extending to many of the suburbs located both north and south of A. Given the tremendous acquisition costs of property required to construct passenger stations and tracks, A attempts to negotiate an agreement with B under which A could utilize either the tracks or property adjacent to those tracks to operate A's light rail service. B remains apprehensive about this arrangement given B's exposure to liability in the event of an accident on its property as well as the possibility of suffering damage to its own property as a result of A's activities. Consequently, A promises to assume liability for damages suffered by A or B in the event of any accidents involving the operation of A's transportation system. B, secure in the belief that its exposure to liability has been limited, executes the agreement with A. A subsequently constructs its light rail system, a substantial part of which operates on B's property. In effect, A's promise to indemnify B facilitates the expeditious and affordable establishment of public transportation in the area.\(^43\) Indeed, A and B's agreement illustrates a contractual arrangement\(^44\)

\(^{43}\) See infra notes 234-247 and accompanying text.

\(^{44}\) While contracts limiting liability, or, more specifically, indemnity agreements, are not homogenous, the agreements among light rail carriers generally provide that the light rail carrier will cover or indemnify, to some extent, the risks incurred by the established carrier. These agreements typically include language similar to the following:

A. "Light Rail" (L.R.) recognizes the fact that operation of its planned rapid transit system adjacent to the "Established Rail" (E.R.) tracks will expose the E.R. to a potential liability in the event of accident. L.R. and E.R. agree that they will devote their best efforts toward providing the E.R. reasonable protection against such liability, prior to the commencement of such operations.

B. Specific areas of protection to be considered for this purpose may include, without limitation: (1) L.R.'s provision of insurance insuring the E.R. against liability for injury to L.R. passengers, property or employees; (2) payment by L.R. for any increase in the cost of existing E.R. insurance coverage attributable to the location of the L.R. operation in proximity to the E.R. operation; and (3) the provision by L.R. of additional insurance
that, regardless of nomenclature,\textsuperscript{45} has been adopted by several major municipal transit systems throughout the United States.\textsuperscript{46}

The value of this bargain is manifold for both \(A\) and the entire local community. The establishment of light rail service in \(A\)'s metropolitan area will provide low cost transportation for area residents. For \(A\), the agreement obviates costly alternatives such as outright purchase of the property from \(B\), or the acquisition of required property through eminent domain. Such acquisition costs

\begin{quote}
coverage for the E.R., such as additional excess insurance. In determining which means of protection is the best suited to the situation, consideration should be given to the limitations, if any, on L.R.'s statutory authority, as it applies to this issue.
\end{quote}

C. L.R., to the extent of insurance coverages hereinbelow described, will protect E.R. because of personal injury, bodily injury, sickness or disease, including death at any time resulting therefrom, sustained by any person or persons, including employees of L.R. and E.R., and any injury to or destruction of property whatsoever, including the loss of use thereof, in any manner or to any degree caused or contributed to by, or arising out of, the presence, use or operation of Route 5 of L.R.'s rapid transit system (hereinafter collectively called the "Transit System") on or about or adjacent to E.R.'s right-of-way or other E.R. property, such duty to protect shall exclude losses arising out of damage or injury caused solely by E.R. operations to E.R. employees or property owned by or in the care, custody or control of the E.R. which shall be borne by the E.R., except where such injury to E.R. employees occurs on L.R. property and injury is made more severe or additional injury is incurred by the presence of L.R. operations, or facilities, such injuries and losses shall be borne by the E.R. and L.R. in equal proportions (50/50 basis) up to the amount of the deductible of insurance as hereinafter provided in Subsection b.(1), and/or by the performance or failure, negligent acts, errors or omissions by L.R. to perform any work in connection with the Transit System's construction, operation, renewal, maintenance, repair, reconstruction or removal and any work which shall be the obligation of L.R. whether due to the negligence of L.R. or E.R. or otherwise.

45. \(A\) and \(B\)'s agreement, which constitutes an indemnity or hold harmless agreement, is also known in the transit industry as a common corridor or shared corridor agreement. While these various nomenclatures may vary in subtlety, they all include a promise by the municipality or authority to indemnify the established rail carrier against any losses attributable to the municipality's or authority's use of the established carrier's property. All of these agreements comprise contracts that limit negligence liability. \textit{See also supra} notes 26-28.

46. In addition to the Washington Metropolitan Area Transit Authority, major transportation systems in other metropolitan areas throughout North America maintain shared corridor or common corridor contracts that include, to some extent, agreements limiting the liability of other major carriers. The transit systems of metropolitan areas such as Dallas, Atlanta, Philadelphia, Chicago, Boston, New York City, New York/Newark, New Jersey, Cleveland, San Francisco, San Francisco, Montreal, and Toronto maintain some form of indemnity agreement with other carriers or entities. \textit{See American Pub. Transit Assoc., Light Rail Transit 14-15} (1989); WMATA Common Corridor Study, \textit{supra} note 15, at 3-1 to 3-2.
can be so extensive as to limit or abort A’s project altogether.\textsuperscript{47} Consequently, the agreement with B may not only accommodate A’s financial goals in establishing its system, but also expedite the establishment of A’s system by avoiding the time consuming modes of acquisition. Given the advantages afforded by light rail transportation,\textsuperscript{48} the expeditious and cost effective construction of A’s light rail system should be of significant benefit to the community.\textsuperscript{49} Thus, the indemnity agreement between A and B ultimately allows this public benefit to come into existence.

Unlike the agreement between X and Y, agreements between parties such as A and B, who are common carriers,\textsuperscript{50} appear to foster an enhanced probability of enforcement.\textsuperscript{51} Yet given the similarities between the two bargains, i.e., the sophistication of the parties and the potential benefit to the parties and society on a whole, the disparity in the probability of enforcement of the two indemnity agreements raises significant questions regarding the efficacy and reliability of indemnity agreements in general. The key may lie in the residual, positive effects of A and B’s agreement. The societal benefit of accessible and affordable public transportation represents a real and significant by-product of this agreement and, perhaps, serves as tacit justification for its enforcement.

Few individuals would argue with the general concern about agreements that contravene clearly articulated public policy concerns. However, compliance with this amorphous goal not only creates inconsistent results with regard to the enforcement of contracts limiting liability, but also fosters considerable uncertainty among parties who may seek to enter such agreements without fearing the possibility that such policies may be violated. Given the nebulous concept of public policy,\textsuperscript{52} the law thrusts agreements

\textsuperscript{47} See WMATA COMMON CORRIDOR STUDY, supra note 15, at 2-2.

\textsuperscript{48} Public transit, which includes light rail transit systems, manifests certain benefits to the localities that it serves. Such benefits include the reduction of automobile congestion and air pollution, the reduced need for expensive highway construction, the reduced need for urban parking facilities, which can be expensive and low revenue-producing, and reduced low-density urban development. See AMERICAN PUB. TRANSIT ASSOC., supra note 46, at 12-13.

\textsuperscript{49} See id.

\textsuperscript{50} See infra note 130.

\textsuperscript{51} See infra part II.F.

\textsuperscript{52} See infra notes 87-88 and accompanying text.
that limit the liability of others into a virtual abyss with neither certainty nor clear delineation of rules governing enforceability.\textsuperscript{53} Notwithstanding an illusion of legitimacy, nearly every indemnity clause faces an uncertain legal future.\textsuperscript{54}

Despite the more modern view that contracts limiting negligence liability are possibly enforceable,\textsuperscript{55} the strict scrutiny\textsuperscript{56} given these agreements due to the decision maker’s\textsuperscript{57} concern for public policy renders such agreements ineffectual. Certainly, strict scrutiny by the courts may discourage parties from initially entering into such bargains. Parties seeking protection may fear that the agreement would never be enforced and, therefore, may leave themselves unprotected. Consequently, the fate of such agreements rests on the nebulous concept of public policy, a notion imbued with subjective standards that are neither certain nor predictable.\textsuperscript{58} Clearly, such a vague standard that governs the scrutiny, if not the enforceability, of contracts limiting liability will lead to inconsistent results and general uncertainty and insecurity among bargainers in the marketplace.\textsuperscript{59} Moreover, the present vagueness in enforcement creates barriers that limit parties’ ability to strike mutually beneficial bargains, and also potentially stymies agreements that would maximize the utility of existing scarce resources and produce a service or product beneficial to the public.

\textsuperscript{53} The concept of public policy, for instance, “is not absolutely invariable or fixed, since contracts which at one stage of our civilization may seem to conflict with public interests, at a more advanced stage are treated as legal and binding.” Pope Mfg. Co. v. Gormully, 144 U.S. 224, 233-34 (1892).

\textsuperscript{54} When indemnity provisions “do or are interpreted to depart from the type of liability that the law would create without the clause, there is the danger of the provision being held inapplicable on the ground that it contravenes public policy, or of being interpreted in a manner not contemplated by the parties.” Potamkin & Plotka, supra note 22, at 361. This problem is particularly troubling given “the antipathy which so many courts have expressed towards hold harmless clauses.” Id.

\textsuperscript{55} \textit{See infra} note 78.

\textsuperscript{56} \textit{See infra} note 86 and accompanying text.

\textsuperscript{57} Courts, legislatures, and other governmental entities such as administrative agencies all play some role in the regulation of the bargaining process. While there are structural differences among these entities, I will, hereinafter, refer to them collectively as the “decision makers.” The choice of this term acknowledges and adopts Professor Kennedy’s view that the distinctions between these entities may be spurious at best. \textit{See} Kennedy, supra note 3, at 564-65.

\textsuperscript{58} \textit{See infra} text accompanying notes 87-88.

\textsuperscript{59} \textit{See} Melvin A. Eisenberg, \textit{The Bargain Principle and Its Limits}, 95 Harv. L. Rev. 741, 742 (1982) (noting the need for a certain coherency in contract and, therefore, the resultant requirement of predictability among bargainers in the marketplace).
II. THE "TRADITIONAL MODEL:" PRESENT RULES THAT GOVERN THE ENFORCEABILITY OF CONTRACTS LIMITING LIABILITY

Voluntary transactions, such as those between $A$ and $B$ and between $X$ and $Y$, often involve an allocation of duties and liabilities. Various legal principles can govern such allocations. Absent any superseding principles, the common law of torts constitutes a primary mechanism that dictates the allocation of duties and liabilities. Traditional tort law doctrine mandates compensation by tortfeasors whose conduct violates the rules of negligence. Parties may attempt to alter the traditional tort law allocation of duties and liabilities with the negotiation of a contractual agreement that redistributes these liabilities.

Utilization of contract principles enables the parties to alter the common law tort allocations of risks associated with their proposed bargains. The employment of contract rules or principles to facilitate consensual agreements resulting from

60. See supra pp. 724-26.
61. See supra pp. 721-23.
63. The cause of action for negligence generally includes: a duty owed by the tortfeasor to the victim to exercise a prescribed standard of care, a commensurate breach of that duty, and a causal link between the breach of duty and the resultant injury. See RESTATEMENT (SECOND) OF TORTS § 281 (1965) [hereinafter TORTS]. Generally, the claimant must prove all of these elements in order to recover under the cause of action of negligence. See id.
64. The hypothetical situations involving $X$ and $Y$ and $A$ and $B$ illustrate bargained-for exchanges that function to adjust the allocation of risks associated with the parties' transactions. For $X$ and $Y$, this allocation remains elusive given the decision makers' skepticism regarding the validity of their agreement. See infra parts II.A-D. Contrarily, $A$ and $B$'s bargain appears more secure. See infra part II.F.
65. The Restatement (Second) of Contracts defines a contract as "a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty." CONTRACTS, supra note 40, § 1. The fundamental purpose of a contract is to preserve the parties' bargain and to serve as a tangible embodiment of the parties' voluntary assent to the contract's terms. See Robert A. Hillman, An Analysis of the Cessation of Contractual Relations, 68 CORNELL L. REV. 617, 653 (1983); Steven R. Salbu & Richard A. Brahm, Strategic Considerations in Designing Joint Venture Contracts, 1992 COLUM. BUS. L. REV. 253, 305.
voluntary transactions comprises a benchmark concept in the neoclassical theory of contract law.67 The parties' use of rules relevant to contract law implicitly reflects their belief that they have provided an enforcement mechanism for their proposed allocation of risk and, commensurately, protected their proposed bargain.68 This situation exemplifies contract law's neoclassical theory, which manifests the goal to support and, to a certain extent, facilitate voluntary transactions in such a way so as to ensure the consensual nature of these agreements while simultaneously requiring the parties to observe a higher standard of fairness.69

Central to the bargain, and a factor that aggrandizes the parties' confidence in the agreement, must be the belief that the bargain will be enforced. The principle that breach of the bargain


While not explored completely in this Article, other theories, e.g., critical analysis, retain and relational contracts, are also probative of the function of contract law and the rules therefrom. See generally Farber, supra (comparing the neoclassical economic model and more recently created models); Feinman, supra note 62 (conducting a critical legal studies analysis of contract law); Feinman, supra (examining the crisis in contract law and theory, and the effect of newly developed theories upon neoclassical scholarship); Charles J. Goetz & Robert E. Scott, Enforcing Promises: An Examination of the Basis of Contract, 89 YALE L.J. 1261 (1980) (discussing promises, their economic implications, and the most efficient means of their regulation); Robert A. Hillman, The Crisis in Modern Contract Theory, 67 TEX. L. REV. 103 (1988) (proposing that modern contract law is best understood not by a single economic theory, but rather by a flexible model that encompasses the entire range of proposed theories); Symposium, Economics of Contract Law, 52 LAW & CONTEMP. PROBS. 1 (Winter 1989) (compiling a series of articles discussing contract law issues).

68. See Goetz & Scott, supra note 67, at 1265 (noting that bargained-for promises tend to maintain the value-enhancing exchanges between the parties). Professors Goetz and Scott further state that "[s]uch promises are thus seen as fully enforceable under the compensation rule in order to protect and encourage value-maximizing resource allocation." Id.; see also PROSSER, supra note 62, at 442.

69. See GILMORE, supra note 66, at 87-90. By holding parties liable when they violate societal standards of fairness, the neoclassical contract theory may be signaling a disintegration of contract and tort law. See id. at 90. In contrast, classical contract law focused on individualism and the maintenance of personal autonomy, see Friedrich Kessler, Introduction: Contract as a Principle Order to FRIEDRICH KESSLER ET AL., CONTRACTS 1, 1-3 (3d ed. 1986); Clare Dalton, An Essay in the Deconstruction of Contract Doctrine, 94 YALE L.J. 997, 1012 (1985); Michael B. Metzger & Michael J. Phillips, Promissory Estoppel and the Evolution of Contract Law, 18 AM. BUS. L.J. 139, 201 (1980), and emphasized the importance of the bargain and the need for consideration in the form of a "bargained-for" exchange. See GILMORE, supra note 66, at 19-21; see E. ALLAN FARNWORTH, 1 FARNWORTH ON CONTRACTS § 2.2, at 61-62 (1990).
will result in an award of compensatory damages buttresses this confidence.\textsuperscript{70} The parties’ attempt to modify their tort law allocations of risk through contract usually results in the formation of agreements of indemnity\textsuperscript{71} or exculpation.\textsuperscript{72} Contracts limiting liability, which principally result from voluntary transactions between parties, tend to illustrate the neoclassical theory of contract law,\textsuperscript{73} notwithstanding certain restrictions placed upon such agreements.\textsuperscript{74}

\textsuperscript{70} In his compelling piece regarding the enforceability of bargain promises, Professor Eisenberg emphasizes that the problem of present contract law focuses on which promises should be enforced, and the extent to which such promises should be enforced. Eisenberg, supra note 59, at 798. He notes that the solution to these questions, if any, must be found in the “paradigmatic bargain principle,” which is grounded in the postulate that “damages for the unexcused breach of a bargain promise should invariably be measured by the value that the promised performance would have had to the plaintiff, regardless of the value for which the defendant’s promise was exchanged.” \textit{Id.} at 798-99. Professor Eisenberg’s explanation also notes that considerations of efficiency and fairness relate directly to this principle. \textit{Id.} at 800. He acknowledges, however, that the bargain principle comprises a difficult theory to implement in the real world, and as such, has led to the rise of unconscionability as a policing mechanism in the transactional process. \textit{Id.} See infra notes 91-95, 173 and accompanying text for a discussion of unconscionability as it relates to the enforcement of the parties’ bargain.

\textsuperscript{71} Indemnity agreements, which constitute one type of contract limiting liability, generally provide for the shift of liability for loss from one individual who generally would be held legally responsible for certain actions, to another individual. \textit{See} Davis, supra note 22, at 517; \textit{see also} Meriam & Thornton, supra note 22, at 845 (recognizing indemnification as a mechanism that shifts loss from one responsible party to another, but also distinguishing the shifting of risks and the attribution of liability due to contribution among joint tortfeasors).

\textsuperscript{72} While indemnity and exculpatory agreements both function to limit the liability of a culpable party, these types of contracts maintain distinctive characteristics. Exculpatory agreements serve to limit or preclude the recovery of damages ordinarily due a victim in a tortious action. On the other hand, indemnity agreements have no applicability to the victim’s right to compensation. Indemnification merely comprises a mechanism that dictates which party in a contractual arrangement will be liable for damages resulting from the victim’s injuries. \textit{See} Goldman v. Ecco-Phoenix Elec. Corp., 396 P.2d 377, 382 (Cal. 1964) (noting that the limitation of liability contained in the parties’ agreement in this case comprises an indemnification agreement in lieu of exculpatory agreement). \textit{See generally} Devlin, supra note 13 (discussing the enforceability of indemnity and exculpation agreements contained in real property leasehold contracts, and providing the distinctions between indemnity agreements and exculpation agreements).

\textsuperscript{73} A significant amount of scholarship has been dedicated to the neoclassical theory of contract law as it relates to the traditional contractual paradigm. \textit{See} Melvin A. Eisenberg, \textit{The Responsive Model of Contract Law}, 36 STAN. L. REV. 1107, 1110-11 (1984). \textit{See generally} ATTIAH, supra note 62 (providing a comprehensive overview of the historical development and modern trends of contractual and promissory liability); Melvin A. Eisenberg, \textit{Donative Promises}, 47 U. CHI. L. REV. 1 (1979) (examining donative promises in the context of administrative and substantive criteria); Eisenberg, supra note 59 (proposing a
Indemnity and exculpatory agreements function much like the concept of insurance. Consequently, indemnity and exculpatory agreements may merit validity given the proliferation of insurance in the marketplace, and the resemblance of those agreements to the concept of insurance. As a premise, these reexamination of the bargain principle and advocating the need for its limitation); Melvin A. Eisenberg, *The Principles of Consideration*, 67 CORNELL L. REV. 640 (1982) (arguing that bargain is not the sole condition of enforceability and advocating a broader conceptualization of the law of enforceability of promises); Lon L. Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799 (1941) (examining the formal and substantive aspects of consideration).

74. *See infra II.B.*

75. The concept of “insurance” represents a mechanism that permits parties to eliminate or minimize their responsibility for risks resulting from perilous exposure or activity. *See Robert Riegel & Jerome S. Miller, Insurance Principles and Practice* 27-29 (5th ed. 1966); *see also Robert Mehr & Emerson Cammack, Principles of Insurance* 11-14 (4th ed. 1952).


77. While this Article will not present a detailed analysis of the insurance issues implicated by contracts limiting liability, the impact of that industry cannot be ignored. By acting as a means of risk-shifting, insurance, in effect, represents “a form of indemnification that provides security against loss by the insured.” *See Devlin, supra* note 13, at 144. Irrespective of its merits, there appears to be a tolerance for insurance against most forms of losses, including the covering of losses sustained by common carriers for their negligence. *See Pettit Grain & Potato Co. v. Northern P. Ry.,* 35 N.W.2d 127, 132 (Minn. 1948) (stating that “[p]ublic policy permits railroad companies to procure insurance to protect themselves against losses which might be sustained in the operation of their business”); *Southern States Coop. v. Northern & W. Ry.,* 247 S.E.2d 461, 464 (Va. 1978) (recognizing “that a common carrier is not prohibited from ‘entering into insurance contracts with duly licensed insurance companies to indemnify [the carrier] against its losses’” (quoting Pennsylvania R.R. v. Kent, 202 N.E.2d 893, 894 (Ind. 1964)). Historically, the courts have justified this position in noting that common carriers are not exempt from liability. *See Pettit Grain & Potato Co.,* 35 N.W.2d at 132 (noting that indemnity insurance “[d]oes not lessen the carrier’s duty to the public imposed by law independent of contract, but, on the contrary, rather increased its means of meeting its responsibility for such negligence”); *see also Buckey v. Indianhead Truck Line, Inc.,* 48 N.W.2d 534, 535 (Minn. 1951) (declaring that an indemnity agreement between a bailor and a bailee does not relieve the bailee of the responsibility for negligent actions, but limits liability “to the extent that the bailor is compensated by insurance”). In most instances, liability tends to be strict. *See Saul Sorkin, Limited Liability in Multimodal Transport and the Effect of Deregulation, 13 Mar. L. Rev. 285, 285 (1989)* (stating that “common carriers of goods have historically been held liable for loss and damage to cargo in their care without regard to fault”); Cindy M. Haerle, Note, *Employer Liability for the Criminal Acts of Employees Under Negligent Hiring Theory: Ponticas v. K.M.S. Investments, 68 Minn. L. Rev. 1303, 1307 n.22 (1984)* (noting that “courts have traditionally imposed absolute liability for employees’ acts in unique employment situations such as common carriers”). Common carriers, then, simply indemnify themselves for their own loss. Consequently, insurance “has no tendency to lessen [a common carrier’s] performance of its duties as a common carrier.” *Pettit Grain & Potato Co.,* 35 N.W.2d at
contracts limiting liability remain valid and, therefore, enforceable.\textsuperscript{78} Despite this general rule of enforceability, the validity of these agreements functions under a significant cloud due to various paternalistic concerns.\textsuperscript{79} Consequently, the viability of these agreements depends upon their intrusion on factors relevant to public policy,\textsuperscript{80} public duty,\textsuperscript{81} or legislation.\textsuperscript{82}

---

133 (equating insurance with indemnification and concluding that neither promotes negligent conduct). The \emph{Petit Grain} court reasoned that the results of negligent acts are “onerous” and “altogether annoying to a railroad.” \textit{Id.} As a result, “[p]articularly in the field of railroads and construction contractors . . . only the extreme of inexperience would harbor the thought that . . . [indemnification or insurance] would operate in the slightest degree as a premium on and so an inducement to” engage in negligent action. Northern P. Ry. v. Thornton Bros. Co., 288 N.W. 226, 228 (Minn. 1939); see generally California Ins. Co. v. Union Compress Co., 133 U.S. 387 (1890) (allowing a railroad to enter an insurance agreement that secures against losses arising from the negligence of its employees); Pryor, supra note 15, at 94 n.12 (rejecting insurance theory for focusing solely on the injured party’s right to payments based solely on a compensatory perspective and arguing that the theory may not adequately encourage deterrence).

78. The prevailing modern view upholds indemnity agreements that exempt a party from ordinary negligence when no public interest is involved and no statute expressly prohibits the provision. See Gardner v. Downtown Porsche Audi, 225 Cal. Rptr. 757, 758 (Cal. Ct. App. 1986). “Ordinary negligence” comprises a breach of duty to exercise ordinary care and can be distinguished from the wanton or willful absence of due care, or the deliberate indifference to the consequences of a particular action. See J.C. Vance, Annotation, \textit{Right of Tortfeasor Guilty of Only Ordinary Negligence to Be Indemnified by One Guilty of Intentional Wrongdoing, Wanton Misconduct, or Gross Negligence}, 88 A.L.R.2d 1355, 1355 (1963 & Supp. 1993). As a rule, exculpatory contracts are valid so long as they do not conflict with public policy or implicate a unique relationship between the parties that militates against enforcement. See Lohman v. Morris, 497 N.E.2d 143, 145 (Ill. App. Ct. 1986); see also Mutual Marine Office, Inc. v. Atwell, Vogel & Sterling, Inc., 485 F. Supp. 351, 354 (S.D.N.Y. 1980) (noting that while disclaimers are disfavored, “there is no reason to reject the disclaimer” when it is unambiguous and the parties were aware of it at the time of the contract); Devlin, supra note 13, at 139.

79. See infra part II.B.

80. E.g., Bisso v. Inland Waterways Corp., 349 U.S. 85, 89-91 (1955). In \textit{Bioso}, the Court announced a rule “invalidating contracts releasing [tug boat operators] from all liability for their negligence” toward their customers. \textit{Id.} at 90. The Court, after noting a long-standing hostile judicial attitude toward such provisions, \textit{id.}, articulated two public policy concerns behind this rule: (1) to discourage negligent conduct by carriers, and (2) “to protect those in need of goods or services from being overreached by others who have power to drive hard bargains.” \textit{Id.} at 91; see infra notes 83-88 and accompanying text.

81. See, e.g., \textit{Lohman}, 497 N.E.2d at 145 (stating that, as a rule, indemnity provisions are valid unless they involve a special relationship, such as that between a common carrier and a passenger who the carrier has a duty to protect).

82. Some statutes may tend to vary the common law liability rules in order to effectuate certain policies. See Torts, supra note 63, § 286. See generally Fleming James Jr., \textit{Statutory Standards and Negligence in Accident Cases}, 11 L.A. L. Rev. 95 (1951) (noting a differing construction of statutory standards related to negligence). By and large, however, many statutes limit the use of contracts limiting liability. See infra notes 120-122.
A. Restrictions Predicated Upon the Concept of "Public Policy"

Restrictions placed upon contracts limiting liability rest on the long-standing belief that agreements that contravene public policy are invalid. Generally, these agreements appear to violate public policy in two ways: the existence of a disparity in bargaining power and the encouragement of reckless conduct. Bargaining power disparity among the parties to a contract is problematic because it may result in an unfair allocation of liability. Furthermore, allowing parties to contract away their liability may encourage or facilitate reckless or negligent conduct. These concerns prompt decision makers to take a critical view of indemnity provisions.

Public policy, however, constitutes an elusive phrase that defies precise definition. It has been viewed as "the community

83. See infra note 98 and accompanying text.
84. 15 SAMUEL L. WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 1751 (3d ed. 1972); see also United States v. Bethlehem Steel Corp., 315 U.S. 289, 326 (1942) (Frankfurter, J., dissenting) (noting that "courts will not enforce transactions in which the relative positions of the parties are such that one has unconscionably taken advantage . . . of the other"); Fitzgerald v. Newark Morning Ledger Co., 267 A.2d 557, 558 (N.J. Super. Ct. Law Div. 1970) (stating that liability provisions are invalid when the parties do not stand on equal footing).
85. A contract exempting a person from liability for future negligent acts is subject to the objection that it tends to induce a want of care . . ." Fitzgerald, 267 A.2d at 558 (quoting 38 AM. JUR. NEGLIGENCE § 8 ).
86. Indemnity provisions "must be construed with every intendment against the party who seeks the immunity from liability" since these provisions "are not favorites of the law." Richard's 5 & 10, Inc. v. Brooks Harvey Realty Investors, 399 A.2d 1103, 1105 (Pa. Super. Ct. 1979); see also Osgood v. Medical, Inc., 415 N.W.2d 896, 902 (Minn. Ct. App. 1987) ("Indemnity clauses are to be strictly construed when the indemnitee seeks to indemnify for its own negligence.").
87. See W.R. Grace & Co. v. Local Int'l Union of United Rubber Workers, 461 U.S. 757, 766 (1983) (noting that public policy must be ascertained "by reference to the laws and legal precedents") (quoting Muschany v. United States, 324 U.S. 49, 66 (1945)); Pope Mfg. Co. v. Gormully, 144 U.S. 224, 233-34 (1892) (stating that the standard of such policy is not absolutely invariable, since contracts at one stage of our civilization may seem to conflict with public interest, at more advanced stages are treated as legal and binding); see also Franklin Fire Ins. Co. v. Noll, 58 N.E.2d 947, 950 (Ind. Ct. App. 1945) (noting the difficulty involved in defining the term "public policy"); Barwin v. Reidy, 307 P.2d 175, 181 (N.M. 1957) (stating that a rule is not "an established rule of public policy" unless its source derives from the Constitution, statutes, and judicial decisions); Pendleton v. Greevor, 193 P. 855, 887 (Okla. 1920) (commenting that the nature of public policy is "uncertain and fluctuating"); Pittsburgh, C., C. & St. L. Ry. v. Kinney, 115 N.E. 505, 507 (Ohio 1916) (observing that "[a] correct definition, at once concise and comprehensive, of the words 'public policy' has not yet been formulated by [the] courts").
common sense and common conscience, extended and applied throughout the state to matters of public morals, public health, public safety, public welfare, and the like. It is that general and well-settled public opinion relating to man's plain, palpable duty to his fellow men ..." This amorphous definition, however, provides little guidance to contracting parties seeking to fashion an acceptable bargain. Notwithstanding its nebulous definition, the rubric of public policy often serves to restrict many contracts that seek to limit the liability of certain parties.

B. Public Policy: Paternalistic Considerations Rooted in Concepts Related to Unconscionability

A significant consideration in the decision makers' evaluation of contracts limiting liability must be paternalistic concerns about a perceived disadvantaged party to the bargain. Specific patterns of conduct of the advantaged party remain intrinsic to the paternalistic concerns regarding the disadvantaged party who functions as the indemnitor. Enforcement of contracts limiting liability may be jeopardized by the assumption that the advantaged parties, indemnitees, will take advantage of their superior bargaining position not only in the negotiation of the agreement, but also in the performance of the contract. The difficulty with enforcement arises from the fact that the indemnitees, who have superior rights under the contract, may behave in an opportunistic fashion with regard to matters related to the agreement.

If the parties exhibit a great disparity in bargaining power, public policy may prompt the decision maker to relieve the weaker

89. Professor Eisenberg indicates that the concept of unconscionability "justifies the limits that should be placed upon the bargain principle" given the need to ensure "the quality of a bargain." Eisenberg, supra note 59, at 779. Consequently, the bargain principle, which on its face appears to be relatively simplistic in design, becomes exceedingly complex and difficult to implement in reality. *Id.* at 799-801. Limitations placed upon the bargain principle by way of mechanisms such as unconscionability not only complicate the decisions as to which bargains decision makers will enforce, but also heightens the administrative costs of enforcing such agreements. *Id.*
90. See generally Timothy J. Muris, *Opportunistic Behavior and the Law of Contracts*, 65 MINN. L. REV. 521 (1981) (noting the problem that arises when one party's conduct is contrary to the other party's understanding of the agreement, though not violative of the explicit terms of that agreement).
partly of its obligation of indemnity under the contract. Supra note 40, § 208 cmt. d; see also Tunkl v. Regents of Univ. of Cal., 383 P.2d 441, 446 (Cal. 1963) (holding that public policy may invalidate a negligence disclaimer when "the party invoking exculpation possesses a decisive advantage of bargaining strength against any member of the public who seeks his services"). For a discussion of Tunkl, see infra notes 113-119 and accompanying text.

92. Northwest Acceptance Corp. v. Almont Gravel, Inc., 412 N.W.2d 719, 722 (Mich. 1987) (identifying an unconscionable bargain as one "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") (quoting Hume v. United States, 132 U.S. 406, 411 (1889)); Meshinsky v. Nichols Yacht Sales, 541 A.2d 1063, 1067 (N.J. 1988) (defining unconscionability as "[t]he standard of conduct contemplat[ing] good faith, honesty in fact and observance of fair dealing") (quoting Kugler v. Romain, 279 A.2d 640, 652 (N.J. 1971)); Rodriguez v. Nachamie, 395 N.Y.S.2d 51, 52 (App. Div. 1977) (describing unconscionability as "an absence of meaningful choice on the part of one of the parties, together with contract terms which are unreasonably favorable to the other party"). Similarly, the West Virginia Supreme Court describes unconscionability as an "overall and gross imbalance, one-sidedness or lop-sidedness that justifies a court's refusal to enforce a contract as written." McGinnis v. Cayton, 312 S.E.2d 765, 776 (W. Va. 1984); see also Williams v. Walker-Thomas Furniture Co., 350 F.2d 445, 449 (D.C. Cir. 1965) (indicating that unconscionability is recognized to include "an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party").

93. Professor Eisenberg notes that unconscionability was considered a bifurcated concept that includes "procedural" and "substantive" unconscionability. Eisenberg, supra note 59, at 752. Procedural unconscionability included basic unfairness in the bargaining process itself. Id. Substantive unconscionability consisted of unfairness in the bargaining "outcome," in other words, the actual terms of the agreement. The distinctions between procedural and substantive unconscionability tended to assist in the reconciliation of that doctrine with the bargain principle. Id. This reconciliation also led to the consideration of "unfair surprise," which became a linchpin in the consideration of unconscionability. Id. at 752-53. Subsequent thought on the subject has indicated that the consideration of unconscionability now encompasses not only consideration of unfair surprise, but also in some cases the examination of the fairness of the terms of the parties' agreements. Id. at 754. See generally Arthur A. Leff, Unconscionability and the Code—The Emperor's New Cause, 115 U. PA. L. REV. 485 (1967) (discussing the problems surrounding the U.C.C.'s unconscionability provision).

94. See CONTRACTS, supra note 40, § 208 cmt. c (emphasizing the concept of oppression as an integral part of the assessment of unconscionability). The Restatement of Contracts recognizes the concept of unconscionability, notwithstanding its basis in the neoclassical theory of contract law. Id. § 208; see FARNSWORTH, supra note 69, §§ 1.8-11 & n.15, at 28-55; John E. Murray Jr., Murray on Contracts § 9 (3d ed. 1990); John E. Murray Jr., The Standardized Agreement Phenomena in the Restatement (Second) of Contracts, 67 CORNELL L. REV. 735, 762-79 (1982) (discussing the relationship between standardized agreements and unconscionability in the Restatement).
Notwithstanding the elasticity of unconscionability, decision makers may be more inclined to invoke the doctrine in situations in which the parties' bargaining positions are disparate and a term of the contract appears onerous or oppressive.

Decision makers may also nullify unambiguous indemnity provisions contained in printed, form contracts. Commonly referred to as "adhesion contracts," these preformed agreements require one party to acquiesce to pre-drafted and possibly unfair terms, typically printed in small type, on a document supplied by a sophisticated business entity. Under these circumstances, decision makers may invoke public policy and, due to paternalistic considerations, shield weaker parties from the consequences of their bargain.

C. Public Policy: Paternalistic Considerations Related to the Protection of Third Parties

Paternalistic concerns relating to the decision makers' evaluations of contracts limiting liability include consideration of the effects of such agreements upon third parties. These concerns for third parties form the basis of the rule that invalidates agreements purporting to exempt tortfeasors from liability arising from their intentional, willful, or wanton misconduct. Anxieties focused upon public welfare and safety weigh against the enforcement of such provisions because "wrong-doing is

95. See U.C.C. § 2-302 cmt. (1990) (stating that "[t]he principle [of unconscionability] is one of the prevention of oppression and unfair surprise . . . and not of disturbance of allocation of risks because of superior bargaining power"); see also ROBERT E. SCOTT & DOUGLAS L. LESLIE, CONTRACT LAW AND THEORY 514-16 (2d ed. 1993) (providing a comprehensive bibliography of materials related to the concept of unconscionability and other factors used to regulate the bargaining process).

96. See 6A ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 1472, at 599 (1962).


98. The cases, with near unanimity, hold that "negligence" does not encompass "willful" or "wanton" behavior and, moreover, that coverage of such conduct by an indemnity clause would violate public policy. Additionally, "reckless disregard of safety" is the modern equivalent of willful, wanton and reckless misconduct. TORTS, supra note 63, § 500; see also KEETON ET AL., supra note 76, § 34, at 213.
discouraged by the imposition of personal punishment.”

Likewise, decision makers would likely strike down clauses that attempt to shield parties from the consequences of their gross negligence.

As a result, indemnity provisions designed to protect indemnitees against the consequences of their own simple negligence encounter significant scrutiny and are viewed with great disfavor. This scrutiny must result from the decision makers’ fear that the indemnitees, given their protection under the

99. Crull v. Gleb, 382 S.W.2d 17, 23 (Mo. Ct. App. 1964) (requiring an insurer to pay the non-punitive damages arising from the reckless conduct of its insured). Although the Crull court held that insurer against the consequences of reckless conduct did not violate public policy (with the exception for punitive damages), this position is not universally accepted. More recently, in Boucher v. Riner, a Maryland appellate court held that “[a] waiver of a right to sue . . . is ineffective to shift the risk of a party’s own willful, wanton, reckless, or gross conduct.” 514 A.2d 485, 488 (Md. Ct. Spec. App. 1986). This policy is intended “to discourage aggravated wrongs.” Id. Other jurisdictions, however, have allowed an indemnitee to contract away liability stemming from reckless conduct—sometimes even criminally reckless conduct. See, e.g., Allstate Ins. Co. v. Schmitt, 570 A.2d 488, 493 (N.J. Super. Ct. App. Div. 1990) (“We discern no public policy prohibition against excluding coverage for risks attendant to reckless criminal behavior.”). The Alabama Great Southern case arose when a collision occurred involving the two railroads. The indemnitee’s train disregarded a stop signal and ran through a closed switch into the path of the indemnitor’s train. See Alabama Great S.R.R. v. Louisville & N.R.R., 127 F. Supp. 363, 365-67 (N.D. Ala.), rev’d, 224 F.2d 1 (5th Cir. 1955). The court ruled that constructing an indemnity provision between the two parties to cover “willful conduct or wanton negligence” would render the clause void as against public policy; and, consequently, “it would to that extent be illegal.” Alabama Great S.R.R. v. Louisville & N.R.R., 224 F.2d 1, 4 (5th Cir. 1955).

100. Generally, “gross negligence” includes negligence which is “substantially and appreciably” greater than ordinary negligence; it represents a major departure from the customary standard of care. TORTS, supra note 63, § 500; Flowers v. Phelps, 956 F.2d 488, 492 (5th Cir. 1992) (noting that Louisiana law prohibits indemnification if damages result from a state official’s gross negligence). But see Hensley v. Erie Ins. Co., 283 S.E.2d 227, 232 (W. Va. 1981) (noting that “[c]ourts also recognize that permitting insurance coverage for acts of gross negligence will not increase the frequency of these acts any more than the original extension of insurance coverage for negligent acts increased their frequency”). For cases in which courts have noted an unwillingness to uphold indemnity agreements that may cover “gross or wanton” negligence, see generally Thomas v. Atlantic Coast Line R.R., 201 F.2d 167 (5th Cir. 1953); Plank v. Atlantic Coast Line R.R., 201 F.2d 170 (5th Cir. 1953).

101. See Heat & Power Corp. v. Air Prods. & Chems., Inc., 578 A.2d 1202, 1206 (Md. 1990) (noting that construing an agreement to indemnify against the indemnitee’s own negligence would be contrary to public policy). But see Manson-Osberg Co. v. State, 552 P.2d 654, 659 (Alaska 1976) (noting a majority rejection of the older view “that indemnity clauses for an indemnitee’s own negligence are unenforceable because they are against public policy”).
agreement, will act in a less precautionary manner. The inescapable corollary to this fear must be the consideration of the effect of reckless conduct upon third parties. The decision makers' concern for third parties appears to escalate proportionately with the extent to which indemnitees attempt to broaden protection from the consequences of their own actions. Such broad protection often comes in the form of a general indemnity provision contained in the parties' agreement, prompting more detailed scrutiny of sweeping indemnity agreements and causing decision makers to restrict the applicable scope of such provisions.

Decision makers look more favorably upon agreements in which indemnitors agree to protect indemnitees from the consequences of the former's sole negligence due to the reduced impact upon third parties. In this instance, the parties simply recognize the tort law notion that one who breaches a duty must compensate the victim. Moreover, this type of agreement benefits the victim by alternatively providing a cause of action sounding in either tort or contract. Under these circumstances, contract law and tort law appear to coexist in relative harmony.

102. Such conduct on the part of indemnitees illustrates the opportunistic behavior that indemnity agreements may arguably promote. See generally Muris, supra note 90 (suggesting methods of controlling opportunistic behavior in such situations).

103. General indemnity agreements are those that do not explicitly include indemnification for an indemnitee's negligence. Examples of "general" clauses include those attempting to exculpate an indemnitee "in any suit at law, . . . from all claims for damages" . . and [even] 'from any cause whatsoever' . . without expressly mentioning an indemnitee's negligence." Rossmoor Sanitation, Inc. v. Pylon, Inc., 532 P.2d 97, 100 (Cal. 1975) (citations omitted).

104. See Amoco Prod. Co. v. Forest Oil Corp., 844 F.2d 251, 255 (5th Cir. 1988) (noting that an indemnification agreement that protects against "all claims" does not include those resulting from the indemnitee's own negligence). The decision makers typically interpret general indemnity provisions as granting indemnitees protection only from damages caused by their "passive negligence." Passive negligence is defined as "mere nonfeasance, such as the failure to discover a dangerous condition or to perform a duty imposed by law." Rossmoor Sanitation, 532 P.2d at 101. "Active negligence," on the other hand, falls outside the scope of general hold-harmless agreements. "Active negligence . . . is found if an indemnitee has personally participated in an affirmative act of negligence, was connected with negligent acts or omissions by knowledge or acquiescence, or has failed to perform a precise duty which the indemnitee had agreed to perform." Id. (citations omitted). Accordingly, the courts often refuse indemnification for affirmative acts of malfeasance. See also infra part II.E. But see Morton Thiokol, Inc. v. Metal Bldg. Alteration Co., 238 Cal. Rptr. 722, 724-25 (Cal. Ct. App. 1987) (allowing the indemnitee to recover despite his active negligence).

105. See supra note 62 and accompanying text.
Certain agreements purport to absolve indemnitees of liability for the concurrent negligence of both parties. These agreements, to a lesser extent, give rise to the decision makers' concerns for the ramifications of these bargains upon third parties. Such agreements governing concurrent negligence tend to draw less skepticism if they result in a reduced impact upon third parties.

D. Public Policy: Paternalistic Considerations Related to the Concept of Public Duty and Operation of Law

Paternalistic concerns also prompt decision makers to reject indemnity agreements that negatively affect a public interest or involve a public duty. These considerations similarly reflect the concern relevant to the agreements' impact upon third parties who constitute a large, societal class or a particular class that commands protection. This scrutiny extends to a variety of situations, including contracts purporting to limit the liability of landlords, employers, or common carriers. In these situations, decision makers appear to guard against the lessening of incentives for safe behavior by indemnitees whose activities directly impact the public welfare.

In a cornerstone opinion that synthesizes the analysis of the public duty implications of indemnity agreements, the California Supreme Court found in Tunkl v. Regents of University of

106. Robert L. Meyers III & Debra A. Perelman, Risk Allocation Through Indemnity Obligations in Construction Contracts, 40 S.C. L. Rev. 989, 992 (1989) (indicating that under concurrent negligence clauses, an indemnitee may recover for his own negligence "so long as the indemnitor is concurrently negligent" but not "for losses sustained as a result of his sole negligence").

107. See id.


109. See Devlin, supra note 13, at 155-56 (concluding that indemnity and exculpatory clauses in residential leases raise public policy concerns because "parties to a residential lease are not likely to be in an equal bargaining position . . . [and] . . . the short supply of affordable housing may force tenants into undesirable contracts").

110. See 6A CORBIN, supra note 96, § 1472, at 598 (noting that employers may not lawfully bargain away their liability to employees for negligently caused harm).

111. See infra notes 130-136 and accompanying text.

112. See infra notes 137-141 and accompanying text.
California that parties "engaged in performing a service of great importance to the public, which is often a matter of practical necessity for some members of the public," may not shield themselves from liability through indemnity provisions.\textsuperscript{113} The Tunkl case arose when a patient, Hugo Tunkl, brought suit to recover damages arising from alleged negligent treatment provided by two physicians at the U.C.L.A. Medical Center. As a condition of his admission, however, Tunkl was required to sign a form releasing the hospital from liability for any negligent conduct by its employees.\textsuperscript{114}

In its ruling, the California Supreme Court identified six specific instances in which public policy and the public interest will not allow a party to exculpate itself from liability: (1) When the transaction "concerns a business of a type generally thought suitable for public regulation"; (2) When "[t]he party seeking exculpation is engaged in performing a service of great importance to the public, which is often a matter of practical necessity for some members of the public"; (3) When "[t]he party holds himself out as willing to perform this service for any member of the public who seeks it, or at least for any member coming within certain established standards"; (4) When "[a]s a result of the essential nature of the service, in the economic setting of the transaction, the party invoking exculpation possesses a decisive advantage of bargaining strength against any member of the public who seeks his services"; (5) When "[i]n exercising a superior bargaining power the party confronts the public with a standardized adhesion contract of exculpation, and makes no provision whereby a purchaser may pay additional reasonable fees and obtain protection against negligence"; and (6) When, "[a]s 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."\textsuperscript{115}

After establishing these guidelines, the court conceded that "while obviously no public policy opposes private, voluntary transactions in which one party, for a consideration, agrees to shoulder a risk which the law would otherwise have placed upon

\textsuperscript{113} 383 P.2d 441, 445 (Cal. 1963).
\textsuperscript{114} Id. at 442-45.
\textsuperscript{115} Id. at 445-46 (citations omitted).
the other party, the above circumstances pose a different situation."\textsuperscript{116} In the six instances outlined above, the California Supreme Court concluded that the releasing party "does not really acquiesce voluntarily in the contractual shifting of the risk."\textsuperscript{117} Moreover, the court stated that an exculpatory agreement need only fulfill some of the six criteria to be invalid as against public policy.\textsuperscript{118} In Hugo Tunkl’s case, however, the court found the release to violate all six tests, concluding that "the hospital-patient contract clearly falls within the category of agreements affecting the public interest."\textsuperscript{119}

In certain cases, decision makers announce restrictions relevant to contracts that seek to limit liability. As a result, certain bargains, by operation of law, may violate a statute or regulation, thereby constituting illegal transactions.\textsuperscript{120} This proscription renders the bargain unenforceable.\textsuperscript{121} Such preemptive prohibitions

\textsuperscript{116} Id. at 446.

\textsuperscript{117} Id.

\textsuperscript{118} Id. at 447.

\textsuperscript{119} Id.; see also Manson-Osberg Co. v. State, 552 P.2d 654, 659 (Alaska 1976) (opining that the court will not give effect to indemnity clauses when doing so would "promote breach of a duty owing to the public at large"); Emory Univ. v. Porubiansky, 282 S.E.2d 903, 905 (Ga. 1981) (invalidating a dentist’s consent clause and holding that "[a] contract between a medical practitioner and a patient must be examined in light of the strong policy of the state to protect the health of its citizens and to regulate those professionals that it licenses").


\textsuperscript{121} For an example of legislation rendering an indemnity agreement unenforceable, see the Louisiana Oilfield Indemnity Act of 1984. \textsc{La. Rev. Stat. Ann.} \textsection 9:2780 (West 1991). This act "declares void and unenforceable those parts of oilfield-related agreements which purport to indemnify an indemnitee against certain types of liability caused by the indemnitee's own negligence or fault." Patrick H. Martin & J. Lanier Yeates, \textit{Louisiana and...
signal the decision makers’ goal to discourage certain transactions due to possible adverse ramifications and to protect society in general from bargains that are deemed improvident.\textsuperscript{122}

\subsection*{E. Manifestation of Paternalism: Strict Construction of Contracts Limiting Liability}

The interpretation or construction of the parties’ indemnity agreement constitutes a significant, discretionary device that clouds the efficacy, and resultant enforceability, of the parties’ transaction. As a general rule, decision makers attempt to construe agreements in such a manner so as to give the parties’ terms a “reasonable, lawful, and effective” meaning.\textsuperscript{123} Yet reasonableness, which connotes objectivity, and lawfulness provide decision makers with latitude to restrict the meaning of an agreement, irrespective of the parties’ true intent. Despite the general rule of enforceability,\textsuperscript{124} contracts that limit liability appear to incur strict interpretation. Strict construction comprises the consideration of the contract’s language, the relationship of the parties, and the agreement’s impact upon societal needs and welfare.\textsuperscript{125}

This tendency to construe indemnity agreements strictly typically involves the implementation of formalistic rules that constrain the applicable effect the agreement. Because the party seeking enforcement of the agreement is likely to be both the

\begin{itemize}
\item \textit{Texas Oil & Gas Law: An Overview of the Differences}, 52 L.A. L. REV. 769, 859 (1992); see also Hanna v. Lederman, 36 Cal. Rptr. 150, 154 (Cal. Dist. Ct. App. 1963) (holding that an exculpatory provision in a residential lease agreement is no defense to a tenant’s claim for damages if the provision violates an ordinance); Cohen v. Mayflower Corp., 86 S.E.2d 860, 860-65 (Va. 1955) (holding that because a void contract is null and binds no one, “an action cannot be maintained for damages for its breach” (quoting 12 AM. JUR. \textit{Contracts} § 10 (1938))).
\item 122. For instance, the California legislature has enacted legislation forbidding indemnification for strict products liability, see \textit{CAL. CIV. CODE} § 2782 (Deering 1986 & Supp. 1994), declaring such provisions “void and unenforceable” as “against public policy”. In \textit{Widson v. International Harvester Co.}, a California appellate court explained that “it would thwart basic public policy behind strict liability to permit indemnification of a strictly liable defendant under a general indemnity clause.” 200 Cal. Rptr. 136, 147 (Cal. Ct. App. 1984).
\item 123. CONTRACTS, supra note 40, § 203(a).
\item 124. See supra note 78 and accompanying text.
\item 125. See \textit{supra}, R. I. & P.R.R. v. Chicago, B. & Q.R.R., 437 F.2d 6, 9 (7th Cir.) (upholding a reciprocal indemnity agreement between two common carriers and noting that the agreement does not threaten to encourage carelessness or unfairly burden a party due to discrepancies in bargaining position), \textit{cert. denied}, 402 U.S. 996 (1971).
\end{itemize}
indemnitee and drafter of the contract, decision makers would typically construe the contract against the drafter-indemnitee.\textsuperscript{126} Judicial disfavor typically results in the interpretation of any ambiguity against the party seeking enforcement.\textsuperscript{127} Furthermore, decision makers require parties to express their intentions in clear and unequivocal language.\textsuperscript{128} A variation of the clear and unequivocal language rule in some jurisdictions is the express negligence standard, which compels decision makers to reject indemnification for a party's own negligence unless the agreement contains specific language covering the express negligence of the indemnitee.\textsuperscript{129} The decision makers' use of rules relevant to the

\textsuperscript{126} Notwithstanding the possibility that the drafter of the agreement may be the best cost avoider in composing the contract, a general rule of construction requires that, in a situation involving a choice of interpretations, decision makers should choose the meaning that goes against the drafter of the agreement. See CONTRACTS, supra note 40, § 206; see also Dickerson, supra note 6, at 142 (noting that the indemnity agreement is strictly construed against the drafter).

\textsuperscript{127} See, e.g., AS J. LUDWIG MONWINCKELS REDERI v. Commercial Stevedoring Co., 256 F.2d 227, 229, 1958 AMC 1563, 1565 (2d Cir.) (recognizing New York's policy of barring "any recovery under an ambiguous indemnity provision or at least requiring a strict construction of the agreement against the indemnitee"), cert. denied, 358 U.S. 801, 1959 AMC 545 (1958); Lackie v. Niagara Mach. & Tool Works, 559 F. Supp. 377, 378 (E.D. Pa. 1983) (noting that "indemnification clauses are generally 'not favored by the law' and are subject to a strict construction compelling an interpretation 'against the party seeking their protection'"); see also Rossmoor Sanitation, Inc. v. Pylon, Inc., 532 P.2d 97, 103 (Cal. 1975) (stating that "indemnification clauses [in employment contracts] are to be strictly construed against the indemnitee in cases involving affirmative acts of negligence on [the indemnitee's] part") (quoting Vinnell Co. v. Pacific Elec. Ry., 340 P.2d 604, 606-07 (Cal. 1959)).

\textsuperscript{128} The general rule of construction was expressed by the Supreme Court in United States v. Seckinger, 397 U.S. 203 (1970): A "contractual provision should not be construed to permit an indemnitee to recover for his own negligence unless the court is firmly convinced that such an interpretation reflects the intention of the parties. This principle, though variously articulated, is accepted with virtual unanimity among American jurisdictions." Id. at 211. The "clear and unequivocal" requirement generally connotes that the indemnity agreement's language must be precise regarding coverage of the indemnitee's negligence. For cases invoking the "clear and unequivocal" language rule, or some variation thereof, see Paul Hardeman, Inc. v. J.I. Hass Co., 439 S.W.2d 281, 285 (Ark. 1969); Heat & Power Corp. v. Air Prods. & Chems., Inc., 578 A.2d 1202, 1206 (Md. 1990); Darin & Armstrong, Inc. v. Ben Agree Co., 276 N.W.2d 869, 872 (Mich. Ct. App. 1979); Ethyl Corp. v. Daniel Constr. Co., 725 S.W.2d 705, 708 (Tex. 1987). But see Amoco Prod. Co. v. Forest Oil Corp., 844 F.2d 251, 256 (5th Cir. 1988) (stating that the key to interpretation is not the precise terms used, but the intent of the parties); Rossmoor Sanitation, 532 P.2d at 103 (relying upon the parties' intent when the explicit language of the agreement is vague); Levine v. Shell Oil Co., 269 N.E.2d 799, 802 (N.Y. 1971) (construing indemnity provisions with respect to the parties' intent despite the absence of clear language in the agreement).
strict construction of the agreement may ultimately frustrate the realization of the parties’ respective bargain, irrespective of the parties’ intentions at the time of contract formation.

F. Paternalistic Considerations Relevant to Indemnity Agreements Among Common Carriers

Upon preliminary examination, contracts that seek to limit liability between common carriers\(^\text{130}\) appear to experience restrictions that are similar to those applicable to agreements formed by other parties.\(^\text{131}\) Because common carriers provide a service to the public, public policy concerns militate against allowing them to bargain away their liability for negligent conduct.\(^\text{132}\) The primary principle that public servants may not exempt themselves from harm caused by their negligence in the performance of their public duties comprises an omnipresent rule governing these agreements.\(^\text{133}\) Accordingly, railroads and other

\(^{129}\) See Ethyl Corp., 725 S.W.2d at 707-08 (rejecting the “clear and unequivocal” language requirement and adopting the “express negligence” standard); see also Singleton v. Crown Cent. Petroleum Corp., 729 S.W.2d 690, 691 (Tex. 1987).

\(^{130}\) A “common carrier” is defined as “one who indiscriminately undertakes, for hire, to transport either commodities or persons, or both.” Sea Ins. Co. v. Sinks, 166 F.2d 623, 625 (7th Cir. 1948); see also Wheeling-Pittsburgh Steel Corp. v. McCune, 836 F.2d 153, 161 (3d Cir. 1987) (noting that because common carriers “undertake[] to carry for all people indifferently,” they can be “regarded in some respects as a public servant”).

\(^{131}\) See supra parts II.A-D (noting the paternalistic concerns that tend to limit the enforceability of certain agreements limiting liability).

\(^{132}\) See Stephan & Sons, Inc. v. Municipality of Anchorage, 629 P.2d 71, 77 (Alaska 1981) (recognizing the possibility that “where the indemnitee is charged with a duty of public service (e.g., a common carrier) and the indemnification is for some neglect in the performance of that duty, the indemnity agreement should not be enforced” because the agreement may be detrimental to society at large); see also Burgess Constr. Co. v. State, 614 P.2d 1380, 1382 (Alaska 1980) (upholding an indemnity provision protecting the state because enforcing the indemnity provision would not significantly affect the state’s duty to the public); see also Keeton et al., supra note 76, § 68, at 482-83; cf. Pennsylvania R.R. v. Kent, 198 N.E.2d 615, 619 (Ind. Ct. App. 1964) (indicating that special agreements adversely affecting the public may contravene public policy and supersede the parties’ right to strike a desirable bargain).

\(^{133}\) See Railroad Co. v. Lockwood, 84 U.S. 357, 382 (1873) (endorsing the notion that “common carriers have public duties which they are bound to discharge with impartiality” and that “they cannot, either by notices or special contracts, release themselves from the performance of these public duties, even by the consent of those who employ them; for all extortion is done by the apparent consent of the victim” (attributing statement to Redfield, C.J.)); Batson-Cook Co. v. Georgia Marble Setting Co., 144 S.E.2d 547, 549 (Ga. Ct. App. 1965); Liberty Highway Co. v. Callahan, 157 N.E. 708, 711 (Ohio
similar common carriers, in the course of conducting their public function, generally cannot insulate themselves from the consequences of their negligence.\textsuperscript{134} Consequently, provisions purporting to indemnify a common carrier for losses arising from "gross negligence, recklessness, wanton and willful misconduct or misconduct warranting the imposition of punitive damages face probable limitation."\textsuperscript{135} Compelling policy objections prevent

\begin{flushright}
Ct. App. 1926); see also Curtiss-Wright Flying Serv. v. Glose, 66 F.2d 710, 712-13 (3d Cir.),
cert. denied, 290 U.S. 696 (1933).

134. See, e.g., Norfolk & W. Ry. v. Adrian Warehouse Indus. Bldg., 657 F.2d 269, 269 (6th Cir. Apr. 17, 1981) (unpublished opinion available only on LEXIS, Genfed library, USAApp file). Norfolk and Western Railway paid damages to a third party who was injured while loading a boxcar adjacent to a dock leased by Adrian Warehouse. \textit{Id.} The railroad, which negligently caused the accident, sought recovery from Adrian pursuant to an indemnification clause in the lease between the two parties. \textit{Id.} In its ruling, the court noted the general rule that a common carrier cannot receive indemnification for the consequences of its own negligence. \textit{Id.} The court indicated, however, that in the present case, the railroad's indemnity agreement did not interfere with its public function and, therefore, did not violate public policy. \textit{Id.; see also} Atlantic Coast Line R.R. v. Coachman, 52 So. 377, 380 (Fla. 1910) (stating that because railroad companies "are created by the state for quasi public purposes, and are thereby affected by a public interest," they must obey the duties of common carriers). For additional commentary regarding a railroad's negligence liability, see generally C.T. Drechsler, Annotation, \textit{Construction and Effect of Liability Exemption or Indemnity Clause in Spur Track Agreement}, 20 A.L.R.2d 711 (1951 & Supps. 1982, 1994); E.R. Tan, Annotation, \textit{Validity, Construction, and Effect of Agreement, in Connection with Real-Estate Lease or License by Railroad, for Exemption from Liability or for Indemnification by Lessee or Licensee for Consequences of Railroad's Own Negligence}, 14 A.L.R.3d 446 (1967 & Supp. 1994).

135. National R.R. Passenger Corp. v. Consolidated Rail Corp., 698 F. Supp. 951, 972 (D.D.C. 1988) (concluding that because neither party had ever discussed or mentioned liability apportionment in cases of gross negligence, recklessness, willful or wanton misconduct, punitive damages awards, or drunken engineers, there was no basis to find that the indemnity provisions covered such instances), \textit{vacated}, 892 F.2d 1066 (D.C. Cir. 1990). Although it vacated the judgment below, the Court of Appeals for the D.C. Circuit did not disturb the district court's analysis relevant to the public policy concerns that are inherent in the evaluation of indemnity provisions. Reversing the lower court's decision due to the requirement for arbitration of the matter, the court stated that it "reverse[s], without addressing either the public policy issue of the substantive issues of contract interpretation that the parties raise. The parties are remitted to arbitration by the terms of their contract, and may raise before the arbitrator their dispute over the scope of the indemnification clause." National R.R. Passenger Corp. v. Consolidated Rail Corp., 892 F.2d 1066, 1067 (D.C. Cir. 1990). For additional authority supporting the limitations placed upon indemnity provisions that attempt to cover gross negligence, see United States v. Seckinger, 397 U.S. 203, 213-15 (1970); District of Columbia v. Royal, 465 A.2d 367, 368-69 (D.C. 1983); Princemont Constr. Corp. v. Baltimore & O.R.R., 131 A.2d 877, 878 (D.C. 1957).

\end{flushright}
decision makers from upholding these provisions even when clear and unequivocal language exists.\(^\text{136}\)

The public policy principles applicable to the railroad industry illustrate the constraints faced by most common carriers.\(^\text{137}\) Passenger safety comprises the dominant concern fueling this skepticism. Congress has explicitly declared that in "regulating the railroad industry, it is the policy of the United States Government [to] promote a safe and efficient rail transportation system by allowing rail carriers to earn adequate revenues" and to "operate transportation facilities and equipment without detriment to the public health and safety."\(^\text{138}\) Moreover, some decision makers refuse to enforce certain common carrier agreements through the strict construction of the carrier’s agreement.\(^\text{139}\)

Similarly, Congress, by way of legislation devoted to the governance of rail programs, manifests the goal to maintain the safe operation of railroads and to minimize damage to property caused by accidents involving common carriers.\(^\text{140}\) Indeed, a theme

\(^{136}\) See National R.R. Passenger Corp., 698 F. Supp. at 970. In National R.R. Passenger Corp., the court held that contract provisions that indemnify against "willful, wanton, reckless, or intentional misconduct . . . are contrary to public policy." Id. at 971. Furthermore, "[w]hile indemnification is particularly disfavored where the indemnitee's activities directly affect the public safety." Id. Thus, the court invalidated the indemnity provision on the grounds that it ran counter to public policy. Id. at 971-72.

\(^{137}\) This Article uses the railroad industry as illustrative of common carrier liability. Other industries would likely face similar constraints in the negotiation of indemnity agreements given their interaction with the public. For additional commentary regarding the negligence liability of other common carriers, such as airlines, see generally C.S. Patrinellis, Annotation, Limitation of Liability for Personal Injury by Air Carrier, 13 A.L.R.2d 337 (1950 & Supp. 1987); Alois Valerian-Gross, Annotation, Limitation of Liability of Air Carrier for Personal Injury or Death, 91 A.L.R. Fed. 547 (1989 & Supp. 1994).


\(^{140}\) Act of July 5, 1994, Pub. L. No. 103-272, § 1(e), 108 Stat. 745, 863 (to be codified at 49 U.S.C. § 20101) (stating that "[t]he purpose of this chapter is to promote safety in every area of railroad operations and reduce railroad-related accidents and incidents").
of public welfare and safety appears to be a ubiquitous objective given the panoply of safety concerns addressed in legislation.\footnote{141}

In certain instances, decision makers curiously seem less anxious about the customary, paternalistic concerns relevant to indemnity agreements among common carriers. When common carriers perform their duties without compensation, for example, the judiciary adopts a more tolerant approach; thus, a railroad may enforce a contract limiting its liability against a passenger riding on a free pass.\footnote{142}

A second exception involves a common carrier performing a service or function that exceeds its obligations.\footnote{143} When a carrier surpasses its public duty and negotiates in a private capacity, the judiciary allows the carrier to bargain away liability. The Supreme Court, for instance, has held that a railroad owes no public duty to a party leasing railroad-owned land.\footnote{144} Similarly,

\footnote{141. See, e.g., 49 U.S.C. § 307(a) (1988) (requiring the Secretary of Transportation to inspect the safety compliance records of each person applying to the Interstate Commerce Commission (ICC) for authority to provide transportation); id. § 10504(c)(1) (noting that even local entities not subject to ICC regulation remain “subject to applicable laws of the United States” related to safety); Act of July 5, 1994, Pub. L. No. 103-272, § 1(e), 108 Stat. 863, 872-81 (to be codified at 49 U.S.C. §§ 20131-20144).

142. See 6A CORBIN, supra note 96, § 1472, at 594 (noting that “[i]f the provision against liability for negligence is contained in a bargain for the rendering of service wholly without compensation, direct or indirect . . . it is valid and enforceable to the same extent as it would be if made by one not engaged in public service at all”). Generally, such provisions are construed as valid against all but gross or wanton negligence. New York C.R.R. v. Mohney, 252 U.S. 152, 157-58 (1920); see also Francis v. Southern Pac. Co., 333 U.S. 445, 448-50 (1948) (noting that waivers of liability contained in free passes of railroad employees are valid and enforceable with regard to culpability for ordinary negligence).

143. Consequently, a railroad may bargain away its liability when acting in a private capacity and leasing railroad-owned land. E.g., Hartford Fire Ins. Co. v. Chicago Ry., 175 U.S. 91, 100-01, 107-08 (1899); see also Princenot Constr. Corp. v. Baltimore & O.R.R., 131 A.2d 877, 878 (D.C. 1957) (indicating that public policy does not bar a railroad from indemnifying itself for simple negligence when it is not acting as a common carrier).

144. Hartford Fire Ins. Co., 175 U.S. at 99. The Hartford decision concerned a lease to a commercial partnership from a railroad of a strip of railroad-owned land adjacent to the train tracks. Id. at 93. The lease granted the partnership permission to erect and maintain a cold storage warehouse on the property. Id. In addition, the lease contained a provision exempting the railroad from liability for any damage to the building or its contents, regardless of which party was at fault. Id. The Court upheld the provision, stating that:

In the case at bar, no one had the right to put a warehouse or other building upon the land of the railroad corporation without its consent; and the corporation was under no obligation to the public, or to the partnership, to permit the latter to do so . . . [B]oth parties knew [the warehouse's] proximity to the track must increase the risk of damages, whether by accident or by negligence, to the warehouse and
decision makers have allowed a carrier to contract freely against its liability when bargaining for the services of an equally sophisticated business entity. In such cases, the carrier is acting outside the scope of its public responsibilities. Decision makers thus treat the carrier as a private entity and will not invoke public policy to shield indemnitors from the consequences of their bargain.

In other situations, the decision makers also surprisingly relax the rule limiting the right of common carriers to contract against their own negligence. The public duty limitation "does not necessarily apply to dealings between connecting carriers, who are in many aspects treated as equals, neither of whom is entitled to any special privileges or protection in the making of contracts."

its contents, by fire set by sparks from the locomotive engines, or by trains or cars running off the track.


145. Santa Fe, P. & P. Ry. v. Grant Bros. Constr. Co., 228 U.S. 177, 189 (1913) (indicating that a liability provision in an agreement between a construction company and a railway was enforceable since "[t]he parties were on equal footing" and the risk of loss "was an item which naturally would enter into the calculations of the parties with respect to the rate to be charged by the Railway Company"); see Chesapeake Beach Ry. v. Hupp Automatic Mail Exch. Co., 48 App. D.C. 123, 129-30 (1918); see also Glaspell v. Ohio Edison Co., 505 N.E.2d 264, 267 (Ohio 1987) (holding that ambiguity in an indemnification clause need not be strictly construed against the indemnitee because the parties were "commercial enterprises of sufficient size and quality as to presumably possess a high degree of sophistication in matters of contract"); Pennsylvania Eng’g Co. v. McGraw-Edison Co., 459 A.2d 329, 332 (Pa. 1983) (upholding an indemnity clause because "this is a case in which a clearly worded indemnification agreement, negotiated between two sophisticated business entities, allocates responsibility for harm without in any respect impairing the ability of injured parties to recover").

146. See Southern States Coop., 247 S.E.2d at 463.

147. See Richard A. Bergjan, D.O., Inc. v. Ohio Bell Tel. Co., 375 N.E.2d 410, 414-15 (Ohio 1978) (stating that in situations when a public utility is granted a monopoly, it should not be allowed to exploit its superior bargaining position to dictate unfair or oppressive terms and conditions; but where "the public utility has no legal or public duty to provide a specific service to its customers, the utility through use of an exculpatory clause may limit its liability for damages caused by its own negligence" (citation omitted)).

148. See General Expressways, Inc. v. Schreiber Freight Lines, 377 F. Supp. 1159, 1161 (N.D. Ill. 1974) (granting an action for recovery under an indemnification clause when the parties were common carriers and "the contract represented an adjustment of the private
If a common carrier, as a favor, grants another party permission to enter the carrier’s property, decision makers hesitate to deny the indemnitee-carrier recovery for its own negligence. Under these circumstances, the judiciary does not perceive indemnification as inviting careless behavior on the part of the indemnitee. Furthermore, as sophisticated business entities, modern common carriers presumably possess relatively equal bargaining power. Decision makers assert that contractual indemnity provisions involving common carriers constitute a private transaction between two bargainers, yet do not alter their duties to the public.

III. CONTRACTS LIMITING LIABILITY: EVALUATING PUBLIC POLICY RATIONALE

The paradox to the decision makers’ strict scrutiny of contracts limiting liability lies in the possible disparate treatment of indemnity contracts among common carriers and similar agreements among other bargainers. There appears to be a certain, perceived hesitancy to invalidate, or some degree of tolerance for, indemnity contracts between common carriers. As previously noted, while indemnity contracts are generally enforceable under modern common law, such agreements are

---

150. *See also* Vinnell Co. v. Pacific Elec. Ry., 340 P.2d 604, 607-08 (Cal. 1959) (vacating the appellate court’s decision that upheld a broad indemnification agreement, yet failing to dispute the lower court’s contention that the railroad should be protected from the consequences of its own negligence). *But see* Southern Pac. Co. v. Morrison-Knudsen Co., 338 P.2d 665, 671-72 (Or. 1959) (upholding the indemnity provision that covered negligence of the indemnitee since the indemnitee’s operation on the indemnitee’s property was for the sole benefit of the indemnitor and the indemnitor was not in a disadvantageous bargaining position).
152. *See id.; infra* part II.A.2.
154. *See supra* part II.F.
155. *See supra* part II.E.
156. *See supra* notes 142-153 and accompanying text.
157. *See supra* note 78 and accompanying text.
subject to strict scrutiny in their interpretation as well as clear limitation in some jurisdictions. However, this rule is not always valid with regard to similar contracts between common carriers. Although a common carrier may not contractually absolve itself of liability related to its public service duties, it may enjoy indemnity against its own negligence if it is contracting with another carrier. Even more striking is the realization that such agreements among common carriers may be enforceable notwithstanding the broad nature of the terms of their agreement.

An understanding of the seeming implied tolerance or, at the very least, reticence to invalidate indemnity agreements among common carriers, requires a close examination of the public policy concerns imbued in such agreements, as noted in the previous section of this Article. These concerns, which include considerations such as bargaining power and the deterrence of future reckless conduct, represent explicit negative factors of public policy—the “prejudicial factors”—that decision makers

158. See supra part II.E.
159. See supra notes 120-122 and accompanying text.
160. See supra notes 130-141 and accompanying text.
161. Common carriers may not limit their liability for negligence related to damages or injuries suffered by passengers or other parties to whom a public service duty is owed. See Lohn v. Morris, 497 N.E.2d 143, 145-46 (Ill. App. Ct. 1986); see also CONTRACTS, supra note 40, § 195(2); supra part II.D.
162. See supra notes 145-147 and accompanying text. Congress formally recognizes the validity of agreements among common carriers whereby the negligence of one carrier may be protected or assumed by the other. See 49 U.S.C. §§ 10730, 11707 (1988).
164. See infra part III.A.2.
165. See infra part III.A.3.
address in determining the interpretation or enforceability of indemnity agreements. Additionally, however, implicit in this evaluation are public policy factors that play an instrumental role in the decision makers' scrutiny of such agreements. Indeed, these implicit factors of public policy—the "constructive factors"—arguably provide a tacit, yet substantial justification for the enforcement of such agreements among common carriers. An examination of these constructive factors of public policy not only supports the enforcement of these agreements among common carriers but also serves as an additional evaluative mechanism that decision makers should use to determine the enforceability of similar agreements of other parties. The evaluation of both the prejudicial and constructive factors of public policy would lead to a much more consistent enforcement rule among all parties who use such agreements and also provide more positive and definitive guidance to future bargainers.

A. Contracts Limiting Liability Among Common Carriers: 
Prejudicial Factors of Public Policy

1. Bargainers' Motivation to Contract: Risk Aversion

Critical to the comprehension of those prejudicial factors of public policy that explicitly govern the decision makers' treatment of indemnity agreements must be the motivation of the parties in the formulation of such agreements. In reference to the hypothetical described in the introduction of this Article wherein A agrees to indemnify B for liabilities arising from B's own conduct, the parties clearly have entered into a voluntary transaction whereby the risk associated with, or related to, A's use of B's property has been shifted to A. The very genesis of this agreement is that, notwithstanding A's compensation to B for any such use, B does not want to assume liability for any damages or liabilities that arise from A's presence on B's property. Indeed B's assent to such an agreement may be predicated upon such a shift of liability. Clearly, B is wary of the risks associated with A's use of, or presence on, its property.

Such an arrangement among the parties illustrates the concept of risk aversion. Most individuals are, to some extent, risk
averse. People’s aversion to risk may help to explain the prevalence of insurance in the marketplace. This factor may also tacitly justify the decision makers’ initial premise that indemnity agreements are valid and enforceable.

Notwithstanding arguments regarding which of the parties would be the more appropriate risk bearer, this shifting of risk from B to A represents the focal point of their voluntary transaction. The validity of A and B’s agreement will be contingent upon whether their voluntary shifting of the risk produces prejudicial factors that prevent enforcement of their agreement. However, the concept of risk aversion is difficult to generalize to all situations. Such difficulties are inherent in transactions involving contracts limiting liability. Risk analyses


167. A clearer illustration of how individuals are risk averse may be the situation in which an individual receives a gift of money. Sam gets $5,000 as a gift, yet Sarah proposes a deal that could possibly increase or decrease Sam’s windfall. Sarah tells Sam that if he agrees to flip a coin and gets heads he will double his money thereby earning $10,000. If Sam flips tails he would lose all of the $5,000. In most instances, individuals such as Sam would refuse Sarah’s wager due to the risk of losing all of the money. Sam’s “disutility” that would result from losing the entire $5,000 is greater than the additional utility obtained if he won the wager. Consequently, Sam’s aversion to risk may urge him to demand additional compensation for accepting such a wager, i.e., that Sarah pay him an additional $5,000 if he wins.

Judge Posner indicates that the distinction between insurance and prevention is “fundamental to the analysis of contract law.” Id. at 103. He states that “[o]rdinary commercial contracts also shift risks, and thus provide a form of insurance. The risk-shifting or insurance function of contracts is related to the fact that a contract . . . by its nature commits the parties to a future course of action; and the future is uncertain.” Id. at 104.

168. See supra note 78 and accompanying text.

169. The identification of the appropriate risk bearer requires the examination of a variety of factors. One may argue that the appropriate risk bearer would be the individual or entity that could more easily afford the risk. Factors relevant to the determination of such an entity would be the cost associated with bearing the risk, i.e., the procurement of insurance; the party who is in the best position to either avoid the liabilities associated with such risks or can more easily or readily obtain information relevant to the avoidance of such risks; and, finally, the transaction costs associated with bearing such risks. In the hypothetical case of A and B, one may argue that B is in the best position to insure against the risks of its own liabilities associated with its own negligence. However, given the fact that A seeks to use B’s property, notwithstanding B’s established use of this property, A should take the necessary precautions required to minimize all possible liabilities arising from the joint use of such property. As a result, A may be forced to assume the cost associated with such risks and to include such costs in the total transaction to obtain use of B’s property.
often fail to account for systemic differences in the degrees of risk aversion due to wealth disparities of the bargainers.\footnote{170}

2. Prejudicial Factors: Bargaining Power Disparity

A primary concern of decision makers regarding contracts limiting liability is the lack of choice on the part of the indemnitor. This dilemma strikes at the very heart of the voluntary nature of the parties' agreement. Here, decision makers will scrutinize the agreement to determine whether the indemnitor would truly assent to such an agreement.\footnote{171} This lack of choice has generally been embodied in the concept of unconscionability.\footnote{172} The lack of effective bargaining power indicates that the indemnitor has no choice but to accept the onerous terms posed by the indemnitee.


\footnote{171} See Graham v. Scissor-Tail, Inc., 623 P.2d 165, 171 (Cal. 1981); see also A & M Produce Co. v. FMC Corp., 186 Cal. Rptr. 114, 126 (Cal. Ct. App. 1982). \textit{But see} Boat & Motor Mart v. Sea Ray Boats, Inc., 825 F.2d 1285, 1291 (9th Cir. 1987) (stressing that "[t]he allocation of risks by superior bargaining power is not unconscionable [rather,] [t]he principle is one of the prevention of oppression and surprise 'and not of disturbance of allocation of risks'" (quoting \textit{CAL. CIV. CODE} \textsection{1670.5} (West 1982))). Similarly, the California legislature identifies the unconscionability doctrine's purpose as the "prevention of oppression and unfair surprise . . . and not of disturbance of allocation of risks because of superior bargaining power." \textit{CAL. CIV. CODE} \textsection{1670.5} cmt. to 1979 ed. (West 1982 & Supp. 1994); \textit{but see also} MURRAY, \textit{supra} note 94, \textsection{96} (suggesting that Llewellyn's purpose in drafting the U.C.C.'s unconscionability clause was to provide a mechanism by which the courts can police contracts).

\footnote{172} \textit{See supra} notes 91-95 and accompanying text.
This lack of choice represents a prejudicial factor that fuels the
decision makers' paternalistic goal of protecting the indemnitee. 173

In the hypothetical situation delineated in the introduction of this Article, 174 both A and B are sophisticated commercial
entities with relatively similar resources required to perfect their
bargain. Both have the necessary means to obtain the information
needed to become fully informed of the facts and circumstances
critical to the bargain. Consequently, A has the power and
intellectual ability to appreciate the requirement inherent in the
indemnity agreement with B. 175 While decision makers have not
always articulated their detailed findings regarding the bargaining
powers of the common carrier entities, 176 the inescapable
conclusion must be that decision makers recognize the common
carriers' equality of position in their respective negotiations of an
indemnity agreement. A and B sit more as equal bargainers than do
a tenant and landlord 177 or a passenger 178 of the common carrier.

Furthermore, the concerns of unequal bargaining position,
and the possible, resultant opportunistic behavior on the part of

173. See supra text accompanying notes 89-95. When decision makers act out of
paternalistic motives, they initiate rule changes that seek to improve the welfare of a party to
the transaction and thereby encourage them to behave in "their 'own real interest.'" Kennedy, supra note 3, at 570. The decision makers' application of unconscionability may
function more from a concern of a bargainer's naiveté, than from a true lack of bargaining
power. Id. at 634 (providing that the difference between "power" and "naiveté" cases is that
the former requires that the beneficiary receive "some weapons [to] fend for herself" and the
latter requires the decision maker to "take the beneficiary under his wing and tell him what
he can and cannot do").


175. In the hypothetical, A and B are corporate entities that are fairly well matched
with regard to personnel and access to information. This situation contrasts with those in
which the bargaining parties do not have the same informational power. See, e.g., Jones v.
Dressel, 623 P.2d 370, 376 (Colo. 1981) (involving a written exculpatory agreement
between a minor and a sky diving company, wherein the court provided four factors relevant
to the enforcement of such agreements: 1) the existence of a public duty; 2) the nature of the
service performed; 3) whether the parties' agreement was entered into fairly; and 4) whether
the language of the agreement was clear and unambiguous); see also Galligan v. Arvitch,
219 A.2d 463, 465 (Pa. 1966) (striking down an exculpatory clause in a preprinted lease
agreement between a landlord and the tenant because "the tenant has no bargaining power
and must accept his landlord's terms").

176. See Chicago, R. I. & P.R.R. v. Chicago, B. & Q.R.R., 437 F.2d 6, 9 (7th Cir.),
cert. denied, 402 U.S. 996 (1971); The Talisman v. New York C.R.R., 57 F.2d 144, 146 (2d
Cir. 1932), rev'd on other grounds, 288 U.S. 239 (1933).

177. See supra note 109 and accompanying text.

178. See supra note 111 and accompanying text.
the indemnityee, should be minimized. Such sophisticated bargainers would be cognizant of the obligation to deal with one another fairly and in good faith. A tacit, yet omnipresent guard against opportunist behavior on the part of the indemnityee in contracts limiting liability must be the proviso that all such agreements will be scrutinized in accordance with the concepts of an implied duty of good faith and fair dealing. B, therefore, would be compelled to bargain fairly and honestly with A. In light of the decision makers’ general approval of indemnity agreements between common carriers, one must assume that the concern for lack of choice or unequal bargaining position is eliminated or at least diminished to the point that paternalistic concerns for the indemnitor should no longer thwart enforcement of the bargain.

179. The decision maker may fear that B, knowing A’s desire to use B’s property and the costly alternatives to such use, may take advantage of such knowledge and negotiate a bargain that would include a broad indemnity agreement that would violate public policy.

180. See CONTRACTS, supra note 40, § 205 (“Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.”)


182. Perhaps decision makers recognize the difficulties and inconsistencies that are inherent in the application of paternalism. See Kennedy, supra note 3, at 633-34.

183. Professor Eisenberg provides four normative situations under which the doctrine of unconscionability typically applies: distress, transactional incapacity, unfair persuasion, and price-ignorance. See Eisenberg, supra note 59, at 754-85. These impediments give rise to the necessity to consider unconscionability in the context of certain bargain situations, and to highlight the imperfections of the competitive marketplace. With the exception of price-ignorance, none of Professor Eisenberg’s normative situations completely relate to the hypothetical situations presented in this Article. The marketplace cannot be considered homogenous and does not often include cost-free information flowing equally to all parties. Consequently, price-ignorance becomes a problem that must be accounted for in the evaluation of the propriety of certain bargains. Id. at 778. When one party has an advantage with regard to determining the price consequences of a transaction, there may be a need for the decision makers to make certain adjustments based upon such superior knowledge. This factor may be inherent in the hypotheticals presented in this Article. One may argue, however, that both parties in the transaction may be equally ignorant of the total price values of their respective bargains in contracts limiting liability. This conclusion may be buttressed

In the case of indemnity agreements between common carriers, the fear of possible breaches of public duty would appear to be congruous with the concern for the encouragement of carelessness or recklessness in situations involving indemnity agreements between other individuals. Decision makers may, in fact, attempt to deter individuals from engaging in reckless conduct through the assumption of liability for losses by third parties, thereby compelling carriers to take the optimum level of precautions to avoid such wrongful behavior.184 Both the breach of public duty and the encouragement of carelessness or recklessness constitute prejudicial factors that would allow or permit an indemnitee to engage in conduct that has negative consequences for third parties.

While not clearly articulated by the decision makers, there may be less concern for the possible breach of a public duty by common carriers who have indemnity agreements with other common carriers.185 While authorities fail to articulate any detailed reasoning regarding the low probability of a common carrier breaching its public duty, factors inherent in the circumstances surrounding such entities contribute to the conclusion that such breaches of duty would not occur. From the standpoint of practicality, it would be contrary to the pecuniary and political interests of the common carrier to breach such a duty.

In the hypothetical situation, although A agrees to indemnify B for B's negligence in their joint operation within the right-of-way, B would not risk engaging in careless or imprudent conduct since any such breach would result in adverse

by the fact that it may be highly unlikely that the parties can accurately predict the true cost of an indemnification that requires the indemnitee to pay all contingencies of an unexpected and unpredictable event. Nonetheless, because both parties are equally ignorant of the costs associated with the transactions in the hypotheticals, Professor Eisenberg's price-ignorance normative situation may not be truly applicable to these hypotheticals.

184. See Steven Shavell, Economic Analysis of Accident Law 127-31, 146-51 (1987). One may argue, though, that the deterrence of conduct through the assignment of remedies under tort law, i.e., compensatory damages, may not be effective and should be replaced. See Stephen D. Sugarman, Doing Away with Personal Injury Law 38-41 (1989).

185. See supra notes 84-85 and accompanying text.
consequences for B’s business. If B engages in reckless conduct in reliance upon A’s promise to cover B’s liabilities, the information generated by such conduct would likely be adverse and disparaging of B and, thus, discourage other individuals from using B as a carrier.\textsuperscript{186} B would likely suffer an exponential reduction of revenue and increased scrutiny from governmental authorities. As a result, B, acting in its own self-interest, would not seek to breach such a duty to the public. Furthermore, various externalities, such as the presence of statutes and regulations governing B’s conduct,\textsuperscript{187} compel B to adhere to its duty to act responsibly in the conduct of its business. Indeed, A and B’s indemnity agreement does not excuse B from adherence to its duty to the public, but comprises an alteration of the business relationship between the two entities.\textsuperscript{188}

4. Prejudicial Factors: The Need for Uniformity and Realism

Given the universality of prejudicial factors in all bargains, decision makers should apply a realistic, evaluative methodology to all indemnity agreements, regardless of the bargainers’ respective identities. Considerations, such as the parity of bargaining positions, that may tend to mitigate the adverse affects of their agreements\textsuperscript{189} should be the primary focus of the question regarding enforceability. For example, in the previously noted hypothetical situation involving X and Y,\textsuperscript{190} one could argue that X and Y, as relatively equal commercial entities, occupy bargaining

\textsuperscript{186} A recent and striking example of the devastating effect of publicity of a common carrier mishap must be the crash of USAir Flight 427 on September 8, 1994. Although no breach of duty by the airline has been found to date, the event and publicity thereof has contributed to a 16\% drop in passenger growth for USAir. One could only surmise that a finding of culpability on the airline’s part would further slow passenger growth. See Dennis Cauchon, \textit{Month-Long Probe Still Yields Few Clues in Pittsburgh Crash}, USA TODAY, Oct. 7, 1994, at A3.

\textsuperscript{187} See supra notes 120-122, 137-141 and accompanying text.

\textsuperscript{188} See Chicago, R. I. & P.R.R. v. Chicago, B. & Q.R.R., 437 F.2d 6, 9-10 (7th Cir.) (noting that the indemnity agreement between the two common carriers did not alter the carriers’ duty to the public, but constituted an adjustment of their private relationship), \textit{cert. denied}, 402 U.S. 996 (1971).

\textsuperscript{189} See supra notes 174-182 and accompanying text.

\textsuperscript{190} See supra pp. 721-23.
positions that are analogous to those of A and B, who are both common carriers.\footnote{191}

While there may be few, if any, specific statutory or regulatory requirements governing Y,\footnote{192} Y's self-interest in preserving the integrity of her business would constitute a disincentive for Y to engage in careless conduct or conduct that breaches a public duty. Notwithstanding a nebulous sense of propriety on Y's part, she would refrain from careless or reckless conduct since such action may be injurious to her business dealings.\footnote{193} Moreover, the decision makers' attempt to adjust for the prejudicial factor of unequal bargaining position may be spurious given the inherent vagueness of the term "unequal."\footnote{194} Consequently, the same analysis of the circumstances involving common carriers who utilize indemnity agreements should be similarly used to evaluate the indemnity agreements of non-common carriers. To implement such a methodology would more accurately assess the impact of prejudicial factors and foster consistency without compromising the interests of third parties.

\textit{B. Consideration of Constructive Factors in Indemnity Agreements}

As previously noted, there appear to be implicit factors that decision makers consider in the evaluation of common carriers' indemnity agreements wherein the indemnitor covers the negligence of the indemnitee.\footnote{195} These implicit factors include the agreement's positive by-products that ultimately benefit third parties. The magnitude of these positive by-products and the

\footnote{191. Note that X's alternatives to the use of Y's property constitute more expensive options. Yet, similar to the situation of A, who also had more expensive alternatives to the use of B's property, expense alone should not constitute a factor that denotes an unequal bargaining position.}

\footnote{192. Y remains subject to general, statutory prohibitions against anti-social conduct that govern all individuals, criminal laws and common law related to breach of duty.}

\footnote{193. Such injury includes negative publicity and possible political ramifications involved with proof of Y's reckless conduct. \textit{See generally} National R.R. Passenger Corp. v. Consolidated Rail Corp., 698 F. Supp. 951 (D.D.C. 1988) (including facts wherein Conrail received negative publicity as a result of its reckless conduct involved in the 1989 derailment that caused significant property damage and loss of life), \textit{vacated}, 892 F.2d 1066 (D.C. Cir. 1990).}

\footnote{194. \textit{See} Kennedy, \textit{supra} note 3, at 614-15 (recognizing that the use of unequal bargaining power to justify intervention is difficult given the lack of precise definitional terms relevant to "unequal power").}

\footnote{195. \textit{See supra} notes part II.A.}
extent to which a significant number of individuals may enjoy the benefits of those by-products arguably bear a direct relationship to the seeming tolerance of indemnity agreements between common carriers. Such implicit positive factors, which are also referred to as constructive factors, provide significant justification for this tolerance. Closer scrutiny of the constructive factors present in the hypothetical transaction between A and B provides substantiation for the decision makers’ tolerance of such agreements.

1. Benefits to Society

As noted in the hypothetical situation between A and B presented in the introduction of this Article, A’s agreement with B facilitates A’s goal of providing fast and affordable public transportation to residents within the municipality. One may posit that the provision of affordable public transportation constitutes a service that benefits the public or society as a whole. While some may argue that public transportation has not been financially self-sustainable and therefore a fiscal drain, such a service, which provides transportation to residents of all socioeconomic backgrounds, comprises an important if not essential municipal service. This constructive factor may indeed formulate the basis of the decision makers’ tolerance of the indemnity agreement between common carriers such as A and B. The consideration of the courts and legislature’s tolerance of the indemnity agreement between parties such as A and B leads to the inescapable

196. See supra p. 752.
197. See supra notes 47-49 and accompanying text.
199. See also Martin Tolchin, Private Concerns Gaining Foothold in Public Transit, N.Y. TIMES, Apr. 28, 1985, at A1 (indicating that mass transit is rarely profitable).
200. While the courts have been silent with regard to consideration of such positive public policy factors, the legislature has indicated concern for such factors. See Act of July 5, 1994, Pub. L. No. 103-272, § 1(e), 108 Stat. 745, 940 (to be codified at 49 U.S.C. § 26102).
conclusion that this agreement’s fostering of a societal benefit, such as public transportation, represents a significant incentive for decision makers to sustain such agreements when prejudicial factors have been ameliorated.

Given the intrinsic, beneficial characteristics of the indemnity agreement between A and B, decision makers should also consider such constructive factors noted in the indemnity agreements of non-common carrier parties as well. In the hypothetical transaction between X and Y, the indemnity agreement certainly would lead to the more expeditious, and possibly less costly, transportation of goods to the general public. One may argue that the agreement’s fostering of such a less expensive alternative of transportation may result in the public’s enjoyment of products at a cheaper cost, assuming that the reduction in transportation costs enjoyed by A would be passed on to the consumers in the form of lower prices. In the most extreme cases, when A markets a product that is important for the sustaining of life, such as medicine or fuel, the constructive factors become even more distinctive. Consequently, constructive factors should be evaluated in the consideration of indemnity agreements between non-common carriers to determine the validity of those bargains.201

2. Promotion of the Optimal Use of Scarce Resources

a. Economic Theory and the Concept of “Efficiency”

An additional constructive factor that decision makers may consider in the evaluation of the validity of the indemnity agreements between common carriers is the agreement’s facilitation of the optimal use of a scarce202 resource, such as land.

201. This presupposes that prejudicial factors as previously identified in this section of the Article have been substantially alleviated. Moreover, such “residual societal benefits” must be identified with a certain degree of particularity in order to justify tolerance of the indemnity agreement between X and Y.

202. The terms “scarce” or “scarcity” connote different definitions among various individuals. Some scholars have defined the term scarcity as a condition whereby an item’s supply is sufficiently limited so that there is not enough to satisfy all needs or desires. See David W. Barnes & Lynn A. Stout, Cases and Materials on Law and Economics 4 (1992). While Judge Posner acknowledges a definition of “scarcity” in terms of limitation of supply, he also indicates that scarcity may be defined in terms of the perceived value of an item, i.e., willingness to pay for a particular item. See Posner, supra note 166, at 34; see also Laurence H. Winer, The Signal Cable Sends—Part I: Why Can’t Cable Be More Like
As noted in the hypothetical transaction between A and B, A obtains the use of B’s property, a scarce resource, at a cost cheaper than the alternative of buying the property outright or resorting to eminent domain. If it is accepted that A’s use is compatible with B’s use of the property, then A and B’s successful, voluntary transaction facilitates or maximizes the optimal use of a scarce resource. A and B’s transaction thereby fosters two non-economic characteristics of efficiency: the minimization of waste and the avoidance of unnecessary effort.

These factors inherent in A and B’s transaction indicate that certain economic principles may provide a tacit basis for the decision makers’ reluctance to invalidate indemnity agreements between common carriers. A and B’s voluntary transaction and other contractual relationships, wherein parties transact agreements that affect the allocation or use of scarce resources, represent bargained-for exchanges of promises that serve to maximize efficient resource allocation. Because the law of contracts


203. “Optimal” has been defined as “the quantity (and corresponding price) at which the social cost of producing one more unit of a good exceeds the social benefit of that unit.” Richard Morrison, Price Fixing Among Elite Colleges and Universities, 59 U. Chi. L. Rev. 807, 828 n.124 (1992). As a corollary to this economist’s definition, the word “optimal” could also connote desirability.

204. See Farber, supra note 67, at 310-12 (noting that the fundamental basis for “neoclassical welfare economics” is the belief that the free market is economically efficient; therefore, resources are allocated to their “highest-valued” uses).

205. While the full range of economic principles that may be applicable to this transaction may be explored in future works on this subject, the basic tenets of economics must be introduced as a possible underlying basis for the sustainment of such indemnity agreements between common carriers. Judge Posner, in defining the positive role of economic analysis of law, indicates that such analysis serves to “explain legal rules and outcomes as they are rather than to change them to make them better . . . . [C]ontracts, bear the stamp of economic reasoning.” See POSNER, supra note 166, at 23. Judge Posner clearly acknowledges those tacit factors that may form the basis for rules such as those governing indemnity agreements. He states, “[o]ften the true grounds of legal decision are concealed rather than illuminated by the characteristic rhetoric of opinions. Indeed, legal education consists primarily of learning to dig beneath the rhetorical surface to find those grounds, many of which may turn out to have an economic character.” Id.

206. See generally PAUL A. SAMUELSON & WILLIAM C. NORDHAUS, ECONOMICS 41 (14th ed. 1992) (noting that voluntary transactions for goods in the market lead to efficient exchanges); see Goetz & Scott, supra note 67, at 1265 (stating that “bargained-for promises support value-enhancing exchanges”). Professors Goetz and Scott further explain that “[s]uch promises are thus seen as fully enforceable under the compensation rule in order to
involves a series of legal rules that preserve the integrity of voluntary exchanges, such rules can also be seen to allocate the benefits and burdens associated with the parties' transactions. Indeed, legal rules associated with contract law arguably promote allocable efficiency through the enforcement of such voluntary exchanges. Accordingly, the decision makers' tolerance of A and B's indemnity agreement may emanate from a belief that such tolerance will promote allocable efficiency. Given the allocation of scarce resources in the hypothetical situation involving A and B, economic theory can assist in determining whether A and B's voluntary transaction should be encouraged, given the benefits provided to A and B and to society as a whole.

207. See Marvin A. Chirelstein, Concepts and Case Analysis in the Law of Contracts 10 (2d ed. 1992) (stating that "[r]ules themselves, if well fashioned, should reflect the arrangement that the contracting parties . . . would have wanted and chosen had they actually gone to the trouble and expense of reaching an agreed position on the particular point at issue"). Chirelstein also indicates that rules should give the parties security to complete the contract even though there has not been agreement on each and every term. Id. (citing Charles J. Goetz & Robert E. Scott, The Limits of Expanded Choice: An Analysis of the Interactions Between Express and Implied Terms, 73 CAL. L. REV. 261 (1985)). See generally Anthony T. Kronman, Specific Performance, 45 U. CHI. L. REV. 351, 370 (1978) (illustrating the manner in which resources may be allocated in voluntary transfers of rights); Richard E. Speidel, Restatement Second: Omitted Terms and Contract Method, 67 CORNELL L. REV. 785 (1982) (discussing the impact of the Restatement (Second) of Contracts § 204 on the contract method).


While additional economic analyses of indemnity agreements may be presented in future articles on this subject, the applicability of such principles appears so strong that they must be introduced in a discussion involving possible tacit toleration of such agreements among common carriers. Economic theory comprises a powerful tool to examine the benefits and also the implications of legal rules. See Posner, supra note 166, at 3. See generally Ronald M. Dworkin, Is Wealth a Value?, 9 J. LEGAL STUD. 191 (1980) (noting that economic principles may provide support for various contract rules and theories).

209. While I am not a dogmatic proponent of law and economics as a primary ideology that justifies legal rules, one must appreciate that economic theory can, as an evaluative tool, assist in the explanation of principles of law. See Goetz & Scott, supra note 67, at 1265 n.17; see also Posner, supra note 166, at 3 n.1, 23-25 (noting that economic theory is "the science of rational choice in a world—our world—in which resources are limited in relation to human wants").
The examination of the hypothetical transaction between A and B reveals that both parties seek to maximize their individual goals. While A wants to obtain property to establish its light rail system in the most inexpensive manner possible, B seeks to maintain its established use of the property and at the same time maximize any value, whether that be monetary, political, or otherwise. The individual goals of A and B, if satisfied in their voluntary transaction, result in the compatible and shared use of a valuable resource, the land or railway track. If a by-product of A and B’s transaction is that a valuable scarce resource receives maximum, compatible usage, then such a result leads to a greater employment of, and benefit from, such a scarce resource.

Proof of the efficiency of A and B’s transaction may be manifest in economic terms by several schools of thought.

210. Perhaps a cornerstone of economic analysis centers on the assumption that people are “rational maximizers of their life’s ends.” See BARNES & STOUT, supra note 202, at 4-5. Consequently, people tend to conduct themselves in a way that will promote their own self-interests. See POSNER, supra note 166, at 3-4.

211. “Valuable resources” can be defined as food, energy, land, time, and labor—items that are finite. Consequently, the allocation of such resources to one purpose often compels the sacrifice of alternative uses. See BARNES & STOUT, supra note 202, at 4.

212. Regardless of the definition of “efficiency,” see infra note 213, rules that promote allocable efficiency have a distinct economic basis. See BARNES & STOUT, supra note 202, at 1-2, 6 (stating that “getting the most from scarce resources available to satisfy society’s needs and wants by allocating them efficiently among competing uses, is the essence of economic principles underpinning such legal rules”); see also Harvey S. Perlman, Interference with Contract and Other Economic Expectancies: A Clash of Tort and Contract Doctrine, 49 U. Chi. L. Rev. 61, 82-83 (1982) (stating that “[i]f allocational efficiency is the objective of contract law, legal rules should encourage persons to search for and to take advantage of more highly valued uses for resources under their command”). It must be noted, as a caveat, that allocable efficiency manifests free market economics in its most prototypical form. This goal may not be totally beneficial if other concerns are not sufficiently addressed, such as the consideration of concerns of indigent individuals. See POSNER, supra note 166, at 441-42.

213. In a law and economics context, “efficiency” has been defined as “the relationship between the aggregate benefits of a situation and the aggregate costs of the situation.” A. MITCHELL POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 7 (1983). Other scholars, however, have found it difficult to articulate a concise definition of the term. In fact, one author notes that “[t]he term ‘efficiency’ has proven to be chameleon-like throughout much of [the past two decades]. Sometimes it has meant Pareto optimality, sometimes a Kaldor-Hicks wealth maximization.” Joseph Sanders, Road Signs and the Goals of Justice, 85 Mich. L. Rev. 1297, 1297 n.4 (1987) (book review).

Others define “efficiency” as clearly synonymous with “Pareto optimality,” or “Pareto efficiency.” Accordingly, from a Pareto perspective “a legal rule is efficient if it induces people to behave in such a way that no one can be made better off (in terms of his or her own preferences) without making someone else worse off. At an efficient point, no mutually
Under the concept of utility maximization,\textsuperscript{214} A and B’s transaction could be considered efficient if the exchange maximizes utility\textsuperscript{215} for both parties. Various arguments can be advanced that this transaction does in fact maximize the utility for both A and B. A, ignoring any potential liabilities from the agreement, receives the use of a scarce resource at a rate much lower than buying such property outright or procuring it through eminent domain proceedings. B, on the other hand, garners a certain degree of satisfaction and happiness from receiving compensation for A’s use of the property, including uninterrupted use of the property for its own purposes and indemnity for any type of liabilities that occur as a result of such joint use. Notwithstanding such observations, A and B’s utility remains difficult to quantify.\textsuperscript{216}

\begin{thebibliography}{9}

\bibitem{215} From a Kaldor-Hicks perspective, however, “efficiency is defined in terms of the aggregative benefits of an activity outweighing the aggregative costs.” Ora F. Harris Jr., \textit{The Automobile Emissions Control Inspection-and Maintenance Program: Making It More Palatable to ‘Coerced’ Participants}, 49 LA. L. REV. 1315, 1345 n.157. (1989). For a more detailed discussion of the Kaldor-Hicks theory, see infra notes 229-233 and accompanying text.

\bibitem{216} “Utility maximization” has been defined generally as “[a] theory assuming that people will always do what is in their best interests.” John E. Noyes, Book Review, 59 N.Y.U. L. REV. 410, 422 (1984). More specifically, according to the utility maximization theory, “if a course of conduct maximizes expected benefits less expected costs, then the rational maximizer will choose to take that course.” \textit{Id.} at 421; see also Charles R. Tremper, \textit{Compensation for Harm from Charitable Activity}, 76 CORNELL L. REV. 401, 424 n.114 (1991). Moreover, the concept is not limited to the economic arena. Indeed, “[s]ome economists define the idea of utility maximization broadly: acting altruistically to help others, for example, can be a rational act designed to maximize unquantifiable feelings of self-worth.” Noyes, \textit{supra}, at 422; see also Michael I. Meyerson, \textit{The Efficient Consumer Form Contract: Law and Economics Meets the Real World}, 24 GA. L. REV. 583, 585-86 (1990) (stating that the utility maximization doctrine presumes that individuals “act to maximize their total benefits minus costs”). Ultimately, “[t]he aggregation of each individual’s utility maximizing decision produces an aggregate social good which the economists refer to as ‘Pareto Optimality.’” Melvyn R. Durchslag, Salyer, Ball, and Holt: \textit{Reappraising the Right to Vote in Terms of Political “Interest” and Vote Dilution}, 33 CASE W. RES. L. REV. 1, 8 n.40 (1982) (citation omitted).


\bibitem{218} BARNES & STOUT, \textit{supra} note 202, at 6; see also POSNER, \textit{supra} note 166, at 12-13.
\end{thebibliography}
One may also argue that A and B's transaction represents an efficient allocation of resources since it may serve to maximize the wealth\textsuperscript{217} of both parties.\textsuperscript{218} In giving the economist's definition of "wealth,"\textsuperscript{219} however, use of wealth maximization to define efficiency, particularly in terms of those agreements that involve considerations of public policy, can be troublesome given the accepted definition that efficiency is defined by willingness, as opposed to an ability, to pay.\textsuperscript{220} Moreover, the premise that people

\textsuperscript{217} The significance of "wealth" constitutes a prevalent concept in the discussions of law and economics, which focuses upon the issue of what constitutes the just distribution of wealth. See, e.g., Posner, supra note 166, at 436-38 (delineating John Rawls' contract theory of distributive justice and criticizing it as being mostly devoid of "operational content"); Guido Calabresi & A. Douglas Melamed, Property Rules, Liability Rules, and Inalienability: One View of the Cathedral, 85 Harv. L. Rev. 1089, 1098-101 (1972).

\textsuperscript{218} "Wealth maximization" is:

the policy of trying to maximize the totality of goods and services, tangible and intangible (leisure is included, for example), weighted by willingness to pay. It is the state of affairs achieved in well-functioning competitive markets. The goal of a wealth maximizing society would be to promote and protect free markets, and to simulate the operation of those markets in settings where natural monopoly, scarcity of information, or externalities prevent markets from operating effectively.


\textsuperscript{219} "Wealth" means "willingness and ability to pay." Mark M. Hager, The Emperor's Clothes Are Not Efficient: Posner's Jurisprudence of Class, 41 Am. U. L. Rev. 7, 23 (1991). Wealth also has been defined as "the satisfaction of individual preferences" or "maximal benefits relative to burdens on individual preferences." William J. Wagner, The Contractual Reallocation of Procreative Resources and Parental Rights: The Natural Endowment Critique, 41 Case W. Res. L. Rev. 1, 161, 171 n.749 (1990). On a societal level, wealth has been called "the aggregate satisfaction of those preferences ... that are backed up by money, that is, that are registered in a market." Richard A. Posner, The Economics of Justice 61 (1981). "Wealth" has also been defined as a "willingness to pay" which is not synonymous with the ability to pay. Posner, supra note 166, at 13.

\textsuperscript{220} Posner, supra note 166, at 13. Despite wealth maximization's initial appeal, the concept is not a universally accepted means of measuring efficiency or evaluating legal policy. For criticisms of wealth maximization, see Jules L. Coleman, Efficiency, Utility and Wealth Maximization, 8 Hofstra L. Rev. 509, 526 (1980) (stating that wealth maximization is limited due to its reliance on prices); Herbert Hovenkamp, Positivism in Law & Economics, 78 Cal. L. Rev. 815, 826 (1990) (noting that wealth maximization is not necessarily a purely positive endeavor and that the term does not necessarily fully capture legislative intent); Anthony T. Kronman, Wealth Maximization as a Normative Principle, 9 J. Legal Stud. 227, 228 (1980) (citing wealth maximization's various negative aspects); Robin P. Malloy, Is Law and Economics Moral?—Humanistic Economics and a Classical Liberal Critique of Posner's Economic Analysis, 24 Val. U. L. Rev. 147, 159 (1990) (concluding that wealth maximization may achieve immoral results); Warren Samuels & Nicholas Mercuro, Posnerian Law and Economics on the Bench, 4 Int'l Rev. L. & Econ. 107, 108 (1984) (noting the limitations of wealth maximization in the determination of rights due to its reliance on price); Ian Shapiro, Richard Posner's Praxis, 48 Ohio St. L.J.
are “rational wealth maximizers” tends to be a somewhat specious assumption in reality.\textsuperscript{221}

b. “Efficiency”—Pareto and Kaldor-Hicks Criteria

A less controversial and, to this author, preferable determinant\textsuperscript{222} of efficiency evidenced in voluntary transactions such as indemnity agreements can be found in the Pareto criteria.\textsuperscript{223} Under the classic scenario, a reallocation of resources, such as $A$ and $B$’s transaction, is said to be Pareto superior to the resource allocation before $A$ and $B$’s transaction if at least one party is better off and no other party is worse off.\textsuperscript{224} A transaction, on the other hand, would be Pareto inferior if the reallocation results in leaving at least one party worse off.\textsuperscript{225}


\textsuperscript{222} My preference for the utilization of Pareto and Kaldor-Hicks criteria connotes my discomfort with other economic determinants of efficiency, such as wealth maximization. While debate concerning the more appropriate determinant may be relentless, it seems clear that any selected economic criteria has normative shortcomings that prompt skepticism. See infra text accompanying notes 227-228, 233-243 (criticizing various economic theories of efficiency).

\textsuperscript{223} POSNER, supra note 166, at 13 (recognizing the controversial nature of wealth maximization as the sole evaluative criteria for efficiency); see also BARNES & STOUT, supra note 202, at 16; see infra text accompanying notes 227-228, 248-251 (criticizing Judge Posner’s wealth maximization theory and economic analysis in general).

\textsuperscript{224} See BARNES & STOUT, supra note 202, at 17; POSNER, supra note 166, at 13.

In the hypothetical transaction involving A and B, one may argue that the parties’ transaction constitutes a Pareto superior reallocation of resources. A is arguably better off because it may establish a light rail system in a much more inexpensive fashion, i.e., shared use of B’s property, than having to purchase the real estate outright. A’s potential savings as far as procurement costs as well as those costs associated with eminent domain, such as negotiations with the land owner and political costs associated with taking private property, serve as further proof that the transaction leaves A in a better position. Although A has agreed to indemnify B against B’s negligence, the availability of insurance and the statutory constraints on B’s negligence minimize not only A’s potential costs, but also damages to third parties that may result from the bargain. While a counter argument to this position could be that potential catastrophic accidents could expose A to significant financial liability as a result of the indemnity agreement, one may also posit that the probability of accidents occurring may be so low as to diminish the significance of such a contingency.

In the case of B, it is better off since A’s use of B’s property will not restrict or otherwise inhibit B’s prior employment of the property. Moreover, the agreement provides B with financial coverage in the event of damages to persons or property resulting from any mishaps due to the common use.

Because a truly Pareto superior transaction must not leave anyone worse off, A and B’s transaction must not adversely affect other parties who are external to the negotiated transaction. For example, passengers on A’s light rail system, other users of B’s property, and adjacent property owners must not be adversely affected by A and B’s transaction. While A remains responsible for those type of liabilities resulting from B’s negligence, there is no guarantee that such coverage by A will fully compensate third parties for losses sustained in any kind of accident occurring as a result of the joint use. This situation may be particularly problematic in cases when there are fatalities and property damage. While monetary compensation can be provided for individuals who suffer such losses, it cannot be determined that this compensation

226. See supra notes 75-77 and accompanying text.
will make the injured individuals whole. This problem emphasizes the difficulty of the Pareto criteria,\footnote{227} possibly diminishing the efficacy of this evaluative model as a reliable indicator of efficiency.\footnote{228}

Given the difficulties associated with the Pareto criteria, the Kaldor-Hicks concept may prove to be a more practical method of evaluating efficiency.\footnote{229} Under the Kaldor-Hicks approach\footnote{230} a transaction could still be efficient notwithstanding the fact that

\footnote{227. Despite its superficial attraction, Pareto optimality, or "Pareto efficiency," is not a flawless economic theory. For instance, "[s]uppose a proposed reallocation of resources would make some people better off and some people worse off. Even if the new allocation makes one million people better off and only one person worse off, Pareto efficiency does not identify which allocation is preferable." Cohen, supra note 225, at 1120. Moreover, [a] more serious problem with the criterion is that it uses the status quo as its point of comparison without assessing the justness of the initial allocation. For instance, suppose that in a two-person society one person has all of the resources and the other has nothing. This grossly inequitable allocation is nonetheless Pareto efficient: the only way to better the position of the disadvantaged person is to take some resources away from the advantaged person and thus to make the advantaged person worse off.}

\footnote{228. One may contend that the Pareto doctrine's unanimity requirement, which requires that all persons benefit from a transaction, renders the doctrine "almost completely useless as a practical evaluative standard." Gregory S. Crespi, The Mid-Life Crisis of the Law and Economics Movement: Confronting the Problems of Nonfalsifiability and the Normative Bias, 67 NOTRE DAME L. REV. 231, 235 (1991).

While in theory one can conceive of Pareto-improvements, such as the removal of an impediment that hinders transactions from taking place in an otherwise 'perfect' market (assuming that the impediment can be removed without cost to any third parties), there are few if any significant measures that can be taken that do not adversely affect someone, somewhere, if only in a nonpecuniary, psychological sense. Application of the Pareto criterion requires that even the most distant and diffuse 'external' impacts of a rule must be assessed because the criterion provides no means of restricting the class of persons impacted or types of impacts that shall be taken into account, or of conclusively determining how to value those impacts.}

\footnote{229. See BARNES & STOUT, supra note 202, at 16; POSNER, supra note 166, at 16 (1992).}

\footnote{230. See Crespi, supra note 228, at 236; see also BARNES & STOUT, supra note 202, at 16 (noting that under Kaldor-Hicks, as long as the "winner gains more than the loser loses, the loser does not actually have to be paid").}
other individuals are not better off, or that some are worse off. A Kaldor-Hicks reallocation remains efficient if the beneficiaries of the deal could compensate the losers fully and still reap a gain, even if compensation to the losers is not proffered.\footnote{See Crespi, supra note 228, at 236; see also Barnes & Stout, supra note 202, at 16 (noting that under Kaldor-Hicks, as long as the “winner gains more than the loser loses, the loser does not actually have to be paid”).}

Consequently, the person who is worse off could be considered fully recompensed if the loser receives enough compensation to indicate that the loser is no worse off after the reallocation. With Kaldor-Hicks, it is neither required nor preferable that all losers in the transaction receive compensation. In fact, in many instances, compensating all losers will be complicated and expensive and, therefore, not efficient.\footnote{See John S. Wiley Jr., A Capture Theory of Antitrust Federalism, 99 Harv. L. Rev. 713, 749 n.167 (1986) (stating that Kaldor-Hicks efficiency “holds one condition to be superior to another if the winners from a change gain enough to be able to bribe the losers to accept the change—whether or not the bribe is actually paid”); see also Madeline Morris, The Structure of Entitlements, 78 Cornell L. Rev. 822, 848 n.62 (1993) (stating that the Pareto definition requires the losers to actually be compensated while under the Kaldor-Hicks definition, the winner need only be able to compensate the loser, though not actually do so). Kaldor-Hicks efficiency frequently is referred to as “wealth maximization.” Crespi, supra note 228, at 236 at n. 19; see Barnes & Stout, supra note 202, at 16; see also Richard A. Posner, Some Uses and Abuses of Economics in Law, 46 U. Chi. L. Rev. 281, 291 (1979) (defining efficiency as “wealth maximization”).}

In the hypothetical transaction of A and B, the potential loser may be anyone adversely affected by A’s operation in B’s right-of-way. While the transaction sets up a mechanism by which A will be responsible for those liabilities, there is no guarantee that such an arrangement would fully compensate an injured third party, especially if the monetary ceiling on A’s insurance policy is insufficient. On the other hand, if A and B had not entered into their transaction and the third party suffered damages as a result of B’s sole operation within the property, the third party’s likelihood of full compensation is no greater. As a result, one may argue that A and B’s transaction, which does not guarantee that no third parties are worse off, provides some degree of compensation for individuals who are adversely affected. Since this compensation would likely be the same regardless of whether A and B both operated in the right-of-way or if only B operated in the right-of-way, one may argue that the reallocation through the indemnity agreement or shared corridor agreement would be efficient.
Like Pareto criteria, the Kaldor-Hicks analysis does not guarantee that the allocation of resources are efficient.\textsuperscript{233} Arguably, $A$ may be a potential loser in the transaction since it has undertaken to assume responsibility for all liability, including $B$'s negligence. Yet, it is unclear whether $A$'s gain under the transaction, access to property and railroad track in an expedient and less efficient manner, will compensate for all of the potential losses that may be incurred as a result of $B$'s negligence. Nonetheless, one may be comfortable with $A$'s situation given the fact that $A$ may procure insurance for such occurrences. Even if $A$ decides to self-insure, the low probability of exposure, together with those externalities that constrain $B$ from engaging in negligent conduct, may connote that $A$'s compensation in the transaction outweighs its costs or liabilities.

c. The Consideration of Cost

No examination of the transaction between $A$ and $B$ can be considered cogent without a discussion of the costs involved in the parties' transaction. In consideration of the economic principles relevant to $A$ and $B$'s transaction, the maximization of benefits relates directly to the minimization of costs associated with the parties' transaction.\textsuperscript{234} Consequently, an optimal allocation of resources may result from any methodology or strategy that minimizes costs.\textsuperscript{235} Considerations of the costs inherent in the parties' transaction are inescapable given the assertion that the bargain between $A$ and $B$, if not bargains among all individuals

\textsuperscript{233} Barnes and Stout indicate that the Kaldor-Hicks concept requires a certain degree of accuracy in the measurement of "appropriate levels of compensation." BARNES & STOUT, supra note 202, at 16. The difficulty then remains as to whether the loser in the transaction between $A$ and $B$ has received enough compensation to ensure a certain level of utility or wealth. The difficulty of this measurement manifests the flaw in the Kaldor-Hicks criteria. As a result, Barnes and Stout prefer Pareto's criteria from a fairness perspective, yet use neither Pareto nor Kaldor-Hicks as justification of the efficiency of allocation of resources in its text. On the contrary, Judge Posner utilizes Kaldor-Hicks' concept as a true gauge of efficiency with regard to transactions and his adoption of Kaldor-Hicks may reflect his preference for the use of wealth maximization to define efficiency. See POSNER, supra note 166, at 13-15.

\textsuperscript{234} See DOLAN, supra note 215, at 14 (defining efficiency as the minimization of costs or expenses).

\textsuperscript{235} Id.
within the marketplace, may be imbued with costs and the opportunistic goals of each of the bargainers to avoid those costs.\textsuperscript{236} Transaction costs may include, but are not limited to, those expenditures involved with $A$ and $B$ getting together, the expenses of the bargaining process itself, and the costs associated with the enforcement of their agreement.\textsuperscript{237} With regard to the ultimate bargain struck by $A$ and $B$, the transaction costs, while difficult to quantify, can be appreciated given the complexity of their agreement.

Because $A$ can readily identify $B$ as the party who possesses the property that $A$ requires for its light rail system, minimal costs will be incurred with regard to the identification of $B$ as the party with whom $A$ seeks to contract. Similarly, barring such externalities as travel and the identification of agents who will negotiate the bargains and the terms between the parties, the costs emanating from the negotiation, such as logistical concerns associated with the bargaining process, should be controllable if they are not extensive. Perhaps the most significant transaction costs between $A$ and $B$ are the time and expertise required to negotiate the terms of the agreement. The bargain between $A$ and $B$ would likely involve intensive consultation among executive officers and the attorneys for both parties. The time spent by these agents will constitute quantifiable costs, which must be taken into account when assessing the viability of the potential agreement between $A$ and $B$.

The transaction costs associated with the enforcement of the bargain between $A$ and $B$ remain difficult to quantify as well. The indemnity agreement between $A$ and $B$ assigns liability prior to

\textsuperscript{236} Given my assertion that most transactions of bargainers involve some types of costs, it remains spurious to examine $A$ and $B$'s transaction as though the parties' face no obstacles to their bargain. The theory posited by Ronald Coase, also known as the Coase Theorem, notes that as long as the bargainers may transact freely, then they will ultimately come to an agreement that not only minimizes costs but also allocates the resources of their bargain to their most valuable uses. See Ronald H. Coase, \textit{The Problem of Social Costs}, 3 J.L. & Econ. 1, 15 (1960); see also Posner, \textit{supra} note 166, at 13-14. Coase notes that as long as there are no obstacles to the party's bargain, then resources will be allocated efficiently regardless of the assignment of rights or liabilities by decision makers. Coase, \textit{supra}, at 2-8. Given the magnitude and extent of the bargain between $A$ and $B$, it would be difficult, if not impossible, to imagine that the parties' transaction would face no costs. Consequently, an analysis under the Coase Theorem, while academically probative, would be unrealistic.

\textsuperscript{237} Polinsky, \textit{supra} note 213, at 12.
the actual occurrence of an event that would give rise to such liability. In the abstract, such an agreement may tend to foster minimal transactional costs since the agreement requires A to assume the cost of liability with regard to any adverse actions on B's part. The minimization of this cost may be considered distinctive given the tendency of decision makers to enforce indemnity agreements between common carriers such as A and B. The costs associated with enforcing A and B's agreement may, however, be greater given the vagueness of the distinction between gross and ordinary negligence, and the decision makers' unwillingness to enforce bargains that foster, or tend to minimize, liability for gross negligence.  

Although the transaction costs incurred by A and B in the negotiation and enforcement of their agreement may be definitive, that factor does not militate against the economic viability of the agreement when viewed in terms of alternative arrangements by A. If A fails to execute an indemnity agreement with B, A will be constrained either to negotiate an agreement for the outright purchase of B's property, or to find alternate routes that would also require some other mode of property acquisition on A's part. If A, as an alternative to an indemnity agreement with B, negotiates the purchase of B's property to establish the light rail system, the transaction costs associated with that alternate arrangement may also be expensive. The agents required to negotiate an outright purchase, i.e., corporate managers, attorneys, real estate specialists, etc., together with the processing of necessary details to make such an acquisition, may be as expensive as, or more expensive than, the bargaining process required to negotiate the indemnity agreement between A and B.

If A entertains an alternate route in order to avoid transacting with B to establish the light rail system, significant transaction costs will be incurred in the identification of other

238. See supra notes 98-100 and accompanying text. Moreover, regardless of the detail and precision of the agreement between A and B, the occurrence of an event that triggers liability may propel the parties to litigate the issue of whether the agreement is applicable to that particular event. See, e.g., National R.R. Passenger Corp. v. Consolidated Rail Corp., 698 F. Supp. 951, 953 (D.D.C. 1988) (noting that the parties disputed whether the indemnity agreement extended to the accident in question), vacated, 892 F.2d 1066 (D.C. Cir. 1990).

239. See supra text accompanying notes 43-47.
property owners whose resources will be required to establish the rail system. Moreover, A will incur substantial costs in the negotiation of individual purchase or acquisition agreements with the various property owners whose real estate is necessary for the construction of the light rail system. Even if A resorts to eminent domain, A’s transaction costs associated with that acquisition will not be significantly minimized. Additionally, the cost to enforce sundry agreements with the possibly numerous other property owners over whose property the alternate route will be constructed may be as costly, if not more costly, than the enforcement of the indemnity agreement between A and B. Although transaction costs are difficult to quantify, their existence in the original transaction between A and B should not impair the economic efficacy of that agreement.

Also to be considered in A and B’s bargain are opportunity costs. Perhaps the best manner in which to view the impact of opportunity costs on A and B’s transaction would be to consider the expense involved if A and B’s indemnity agreement were prohibited by the decision maker. Under such a situation, B, who is risk averse, would be reluctant to allow A to utilize B’s property for the light rail system. Although this would minimize liability on B’s part, B would lose the requisite revenue that it would ordinarily receive from A if B had allowed A to use its

240. See supra text accompanying notes 47.
242. “Opportunity cost” is defined as “the benefit foregone by employing a resource in a way that prevents its use for something else.” Andrew R. Schein, Note, Attorney Fees for Pro Se Plaintiffs Under the Freedom of Information and Privacy Acts, 63 B.U. L. REV. 443, 459 n.98 (1983) (quoting RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 3 (2d ed. 1977)). One legal scholar draws upon the lyrics of singer Billy Joel to illustrate the opportunity cost concept: “‘Opportunity cost,’ can be defined as the price that you pay for the things that you might have done.” Ian Ayres, Analyzing Stock Lock-Ups: Do Target Treasury Sales Foreclose or Facilitate Takeover Auctions?, 90 COLUM. L. REV. 682, 688 n.19 (1990) (quoting BILLY JOEL, ONLY THE GOOD DIE YOUNG, on THE STRANGER (1977)).
243. This analytical strategy emanates from the view that the opportunity (A’s joint use of B’s property) afforded by the enforcement of A and B’s indemnity agreement would be less costly (particularly to A) than any alternative (A’s procurement of B’s property or the rerouting of the light rail system). Consequently, the opportunity provided by the execution and enforcement of A and B’s agreement represents the “most valuable alternative that must be forsaken to undertake a given act.” ARMEN ALCHIAN & WILLIAM R. ALLEN, EXCHANGE & PRODUCTION 464 (3d ed. 1983).
244. See supra notes 166-167 and accompanying text.
property. B would also lose, if the public supported A’s project, a certain amount of goodwill.

The opportunity costs to A as a result of the decision makers’ refusal to enforce an indemnity agreement between A and B flows naturally from B’s refusal to allow A to utilize B’s property. Because A can no longer use B’s property, A must resort to a more expensive alternative of either purchasing B’s property outright, or selecting an alternate route for the rail system that would require the acquisition of the property of others.245 Third parties, such as potential passengers of the light rail system, will likely incur more expensive light rail service due to A’s inability to enter into a shared corridor agreement with B. This situation may also result in the probable delay of construction of the system and possibly the reduction or elimination of rail service altogether due to the expense of alternate property acquisition on A’s part.246

Opportunity costs can also be viewed in light of the enforcement of A and B’s indemnity agreement. For example, if a decision maker enforces A and B’s indemnity agreement, A and B, absent any adjustment of the light rail system’s path or extent of service, will likely forego the alternative of operating in separate properties, thereby maximizing their exposure to one another’s possible negligent acts. As a result, third parties, in the situation when A and B’s agreement is enforced, will lose the opportunity to enjoy a presumably safer light rail system that would not operate in a shared corridor situation.247

The existence of opportunity and transaction costs remains evident regardless of whether or not the indemnity agreement between A and B is enforced. Inherent in the consideration of

245. See supra notes 43-49 and accompanying text.
246. One may argue, however, that the construction of the light rail system in a non-shared corridor property would result in a per se safer system since two common carriers will not operate within the same proximity. However, this increased degree of safety must be balanced against the probable increased cost of service due to more extensive acquisition requirements by A, and the possibility that such extensive acquisition costs may cause A to abandon the project altogether.
247. This opportunity cost to third parties presupposes that such parties would be exposed to significant recklessness if A and B’s indemnity agreement was enforced. However, this assumes that there are not externalities, such as other statutes or codes or the maintenance of consumer confidence, that would prevent or discourage B from negligent conduct likely to result in injuries to third parties. See supra notes 186-188 and accompanying text.
either situation, however, is the fact that such costs, while identifiable in concept, remain difficult to quantify. The inescapable conclusion is that these costs remain innate in any bargain that $A$ and $B$ might transact. Moreover, these costs exist in some form regardless of whether $A$ and $B$ negotiate an indemnity agreement. Because all transactions will have some measure of transaction and opportunity costs, the existence of those costs should not diminish the economic viability of those agreements.

d. Economic Analysis—Not a Panacea, Yet Probative

Although economic theory provides a useful tool to evaluate the efficiency of $A$ and $B$'s transaction, it is not definitive.\footnote{248} To a certain extent, economic analysis requires the use of simplified assumptions relevant to human behavior.\footnote{249} Such simplification arguably may lead to unrealistic models of human behavior and also undermine the neutrality of the analysis.\footnote{250} Moreover, bargainers seldom possess perfect information and

\begin{footnotesize}


\footnote{249. Critics of the law and economics movement, however, contend that applying strict economic standards to diverse legal problems is an unrealistic approach that produces flawed results. Arthur A. Leff, Economic Analysis of Law: Some Realism About Nominalism, 60 Va. L. Rev. 451, 470-74 (1974) (arguing that the law and economics movement relies on the faulty premise that, in any given situation, a person will act to maximize personal utility). See generally Robert C. Ellickson, Bringing Culture and Human Frailty to Rational Actors: A Critique of Classical Law and Economics, 65 Chi.-Kent L. Rev. 23 (1989) (proposing that legal principles be evaluated from not only an economic perspective, but a psychological and sociological perspective as well); Cohen, supra note 225 (rejecting the role of economic analysis in Posner's judicial decisions); Note, supra note 6 (rejecting the traditional law and economics contention that an unregulated market reaches efficient results).

\footnote{250. Various scholars have criticized Judge Posner's economic analyses of law. Cf. Polinsky, supra note 213, at 1657-59, 1680-81 (criticizing Posner for failing to state explicitly that the "strict assumptions of his economic models are unrealistic and, therefore, comprise an unsatisfactory basis for the extrapolation to actual human behavior"); John J. Donohue III & Ian Ayres, Posner's Symphony No. 3: Thinking About the Unthinkable, 39 Stan. L. Rev. 791, 812 (1987) (reviewing Posner, supra note 221) ("[E]conomic reductivism systematically favors Posner's conservative platform.").}

\end{footnotesize}
complete rationality, and often incur significant transaction costs.\textsuperscript{251}

Yet, the implementation, to a degree, of economic analysis can be useful to prove that \( A \) and \( B \)'s transaction manifests factors that demonstrate an efficient allocation of a scarce resource, such as property. Other discussions in the context of economic analysis include the question of which distributive concerns should govern choices about the legal and economic structure of society.\textsuperscript{252} This idea may certainly apply to contracts limiting liability, given the potential resource allocations inherent in these transactions.\textsuperscript{253} While decision makers have failed to articulate an explicit recognition of economic influences within the bargain, a thorough examination, inclusive of economic factors, leads to the inescapable conclusion that such a tacit by-product supports the tolerance of the indemnity agreement. Given these tacit, constructive factors demonstrated in \( A \) and \( B \)'s transaction, decision makers should also consider such factors in similar agreements of other parties.

The hypothetical transaction involving \( X \) and \( Y \) illustrates this point. \( X \) and \( Y \)'s transaction is similar to \( A \) and \( B \)'s in terms of the efficient allocation of a scarce resource, i.e., property. While \( X \) is not of the same magnitude as \( A \) as far as the ability to cover the liabilities of the landowner, certainly \( X \) is in no appreciably worse position than \( Y \) to obtain insurance or to self-insure against such liabilities. More importantly, the fostering of \( X \) and \( Y \)'s indemnity agreement may result in the supply of cheaper and more plentiful widgets, since \( X \) may employ the less costly alternative of utilizing \( Y \)'s property. Consequently, \( X \) and \( Y \)'s transaction, which has not traditionally received uniformly favorable judicial or legislative

\textsuperscript{251} See generally Farber, supra note 67 (exploring the neoclassical model of contract law as it relates to microeconomic theory, and ultimately providing a more comprehensive theory of the limits on freedom of contract).

\textsuperscript{252} See POLINSKY, supra note 213, at 124-27 (proposing that legal rules are inefficient as a means of redistributing wealth and that the tax and transfer system would be preferable). The debate concerning the import and use of distributive concerns constitutes a normative question and, thus, does not specifically address how the rules of contract law under the neoclassical theory would affect individuals who seek to enter into agreements such as indemnity contracts.

\textsuperscript{253} See supra text accompanying notes 234-247 (providing an example of resource allocations in indemnity contracts between common carriers).
treatment as the bargains entered into by parties such as A and B, should be similarly judged.

IV. CONCLUSION

Freedom of contract does not, and should not, comprise the solitary goal of decision makers who examine the enforceability of bargained-for exchanges. Indeed, impediments in the bargaining process, namely those concepts that evidence extreme opportunism within the bargaining relationship, require a certain degree of scrutiny from decision makers with regard to the potential enforcement of agreements.\textsuperscript{254} The use of mechanisms to check bargains that have been procured through overt opportunistic behavior remains a steadfast requirement to ensure that truly consensual agreements will be encouraged and enforced.\textsuperscript{255} Even those who argue the absolutist position of the supremacy of the freedom of contract doctrine must also recognize that “freedom” includes the discretion \textit{not} to enforce agreements.\textsuperscript{256}

While the concept of freedom of contract has eroded to the point of becoming an oxymoron, it should not be discarded as a foundation for voluntary transactions. The acknowledgment of the vulnerability of the freedom of contract doctrine does not diminish the need for decision makers to maintain as their focus the enforcement of bargains to which parties have freely and willingly consented. The concept of consent, in fact, represents a corollary, if not an extension of, the notion of freedom of contract. Yet, such willing consent includes a moralistic underpinning that ensures that such bargains are truly consensual.\textsuperscript{257}

\textsuperscript{254} See supra part II.A-E. and accompanying text.

\textsuperscript{255} See Eisenberg, supra note 59, at 748-50; supra notes 60-82 and accompanying text.

\textsuperscript{256} See Kennedy, supra note 3, at 565-70 (acknowledging that the freedom of contract not only embodies the right to strike bargains in accordance with one’s own desired goals, but also the discretion of decision makers not to enforce such agreements).

\textsuperscript{257} See Randy E. Barnett, A Consent Theory of Contract, 86 COLUM. L. REV. 269, 299 (1986) (arguing that the “consent theory” constitutes a “moral component that distinguishes valid from invalid transfers of alienable rights”). Professor Barnett opines that the consent theory of contract not only provides a foundation for the “objective” approach to the determination of contractual intent, but also constitutes a more effective theory to substantiate contractual obligations. Id. at 291-94, 296-309. Professor Barnett promotes the use of the consent theory of contract, which takes into account an objective approach to discerning the contractual intent, and also tends to manifest a clear sense of enforceability that avoids the need to deal in vague concepts.
The focus of legal rules should be to foster such transactions and to ensure that parties enjoy a certain degree of certainty and surety with regard to the bargains which they have entered. Adverse by-products of unfettered freedom of contract, namely unconscionability in the bargaining process and adverse affects on third parties such as an encouragement to reckless conduct, require careful consideration of such prejudicial factors. Yet, consideration of prejudicial factors alone has led to inconsistent results with regard to indemnity agreements among various parties, and fails to provide any homogeneous and reliable signals to individuals who utilize these agreements.

The fact that decision makers display a certain degree of tolerance for indemnity agreements among common carriers reflects both satisfaction with the minimization of prejudicial factors, and tacit adoption of constructive factors inherent in such agreements. Constructive factors such as positive societal by-products of the parties' agreement and the possible efficient allocation of resources emanating from the transaction represent a significant, albeit implicit underpinning of such agreements. The recognition of these constructive factors in indemnity agreements among common carriers begs the question: Why not consider such factors in all indemnity agreements? Indeed constructive factors, which tend to produce positive benefits for an unspecified number of third parties, should be a common consideration by courts and legislatures in formulating legal rules governing voluntary transactions. A more explicit acknowledgment of these factors by decision makers, together with the consistent evaluation of such factors in all agreements, will lead to more consistent results and greater security among potential bargainers.

I believe that Professor Barnett's consent theory represents a moralistic refinement of the freedom of contract notion and is closely related to the neoclassical form of contract theory. See supra notes 66, 70. As a result, his depiction of the consent theory complements the evaluative process decision makers should implement in the review of contracts limiting liability. Although the decision makers' consideration of constructive factors may not relate directly to the consent theory of contract, the consideration of prejudicial factors that tends to predominate the decision makers' evaluation of such agreements would relate directly to the concept of consent.