Has The Contract Clause Counter-Revolution Halted? Rhetoric, Rights, and Markets in Constitutional Analysis

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Introduction

In 1978, the Supreme Court chose *Allied Structural Steel v. Spannaus*,[1] a Contract Clause[2] case, to suggest a fundamental departure from its post-Depression approach to economic regulation.[3] Five years later, in *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*,[4] the Court employed another Contract Clause case to exhibit second thoughts.[5] *Allied Structural Steel*, the earlier case, was frighteningly "reminiscent of the *Lochner* era."[6] According to dissenting Justice Brennan, the majority "undermine[d]" forty years of Contract Clause jurisprudence.[7] *Allied*

1. 438 U.S. 234 (1978).

2. U.S. CONST. art. I, § 10, cl. 1 ("No State shall . . . pass any . . . Law impairing the Obligation of Contracts . . . .").

3. Contract Clause cases form appropriate occasions for judicial reconsideration of the constitutional structure of economic regulation. While the Fourteenth Amendment Due Process Clause has overshadowed the Contract Clause in postwar jurisprudence of economic regulation, the Contract Clause historically has formed the constitutional basis by which that balance has been struck. The Contract Clause has been called the "major restraint on state economic regulation" in the first century of government under the Constitution. G. GUNTHER, CASES AND MATERIALS ON CONSTITUTIONAL LAW 554 (10th ed. 1980). Although by its terms the clause restrains only state regulation, in the wake of the heightened scrutiny of retroactive economic legislation required by *Allied Structural Steel*, several circuit courts considered whether to apply its revived Contract Clause principles to the federal government through the Fifth Amendment. *See* A-T-O, Inc. v. Pension Benefit Guar. Corp., 634 F.2d 1013 (6th Cir. 1980); Northwestern Nat'l Life Ins. Co. v. Tahoe Regional Planning Agency, 632 F.2d 104, 106 (9th Cir. 1980); Nachman Corp. v. Pension Benefit Guar. Corp., 592 F.2d 947 (7th Cir. 1979), *aff'd on statutory grounds*, 446 U.S. 359 (1980); *see also* City of New Brunswick v. Borough of Milltown, 686 F.2d 120, 134 (3d Cir. 1982), *cert. denied*, 459 U.S. 1201 (1983) (analyzing federal acts as if Contract Clause governs); *cf.* United States Trust v. New Jersey, 431 U.S. 1, 60 (1977) (Brennan, J., dissenting) (Due Process Clause jurisprudence could incorporate Contract Clause principles); Leedom v. International Bhd. of Elec. Workers, 278 F.2d 237 (D.C. Cir. 1960); Battaglia v. General Motors Corp., 169 F.2d 254, 261 (2d Cir. 1948) (due process examination of federal impairment of contract, citing Depression-era Contract Clause case). *But cf.* Peick v. Pension Benefit Guar. Corp., 724 F.2d 1247, 1264-65 (7th Cir. 1983) (heightened Contract Clause scrutiny inapplicable to Fifth Amendment due process case absent federal self-dealing) (dictum). *See also infra* note 5.

4. 459 U.S. 400 (1983).

5. Following *Energy Reserves*, the Supreme Court suggested that the relaxed scrutiny of state legislation under the Contract Clause undertaken in that decision would not form a significant hurdle if applied to Congress through the Fifth Amendment. Pension Benefit Guar. Corp. v. R.A. Gray & Co., 104 S. Ct. 2709 (1984) (holding retroactive federal economic legislation constitutional, refusing to apply heightened judicial scrutiny regardless of the Contract Clause standard).

6. L. TRIBE, AMERICAN CONSTITUTIONAL LAW 44 (Supp. 1979).

7. 438 U.S. at 259-60 (Brennan, J., dissenting) (linking revived Contract Clause with substantive constitutional review of economic legislation); *see also* United States Trust Co. v. New Jersey, 431 U.S. 1, 60-61 (1977) (Brennan, J., dissenting).

Structural Steel arguably promised to renew *Lochner* era[8] constitutional supervision of economic legislation by beginning a "process of reinvigorating" the Contract Clause.[9] This would overthrow the uncritical approach to economic regulation characteristic of constitutional interpretation since the 1930's.[10]

The Supreme Court abruptly reversed direction five years later in *Energy Reserves*. *Energy Reserves* accepted legislative interference with a private bargain for explicit redistributive purposes. Where *Allied Structural Steel* required that state legislation address "an important general social problem"[11] before allowing interference with contractual expectations, *Energy Reserves* provided a less precise and more relaxed standard of Contract Clause scrutiny. It merely required that the legislation have a "significant and legitimate public purpose."[12] Part I of this Article explores these contrasts in detail.

This Article analyzes the differences between the *Allied Structural Steel* and *Energy Reserves* decisions in terms of alternative judicial visions of economic regulation. *Allied Structural Steel* embodied a view of economic life that recalls the *Lochner* era by protecting private rights more than public needs and by assuming that markets successfully allocate goods. In contrast, *Energy Reserves* returned to the deeply entrenched postwar view of economic regulation by acknowledging that markets unsuccessfully handle important public problems. These cases renew the judicial controversy between alternative views of economic

8. Lochner v. New York, 198 U.S. 45 (1905), invalidated a state law setting maximum hours for bakery workers. Its progeny represent a period of strict judicial scrutiny of economic regulation under the Due Process Clauses. During the *Lochner* era of constitutional interpretation, progressive and redistributive social and economic legislation was invalidated under the Due Process Clauses of the Fifth and Fourteenth Amendments in order to immunize contractual bargains from collateral government attack. *See generally* L. TRIBE, AMERICAN CONSTITUTIONAL LAW 435 (1978).

9. G. GUNTHER, *supra* note 3, at 567; *see also* Schwartz, *Old Wine in Old Bottles? The Renaissance of the Contract Clause*, 1979 SUP. CT. REV. 95, 96; *cf.* B. SIEGAN, ECONOMIC LIBERTIES AND THE CONSTITUTION 237-38 (1980) (*Allied Structural Steel* accomplishes little of the judicial policy change necessary to protect economic liberties). The potential breadth of a reinvigorated Contract Clause is suggested by the wide range of contracts affected by state action and tested under the Contract Clause since 1982. *See, e.g.*, *Energy Reserves*, 459 U.S. at 400 (natural gas supply contract); Don't Bankrupt Wash. Comm. v. Continental Ill. Nat'l Bank & Trust Co., 696 F.2d 692 (9th Cir.), *appeal dismissed*, 460 U.S. 1077 (1983) (municipal bond); Utah League of Insured Sav. Assn's v. Utah, 555 F. Supp. 664, (D. Utah 1983) (due on sale clause in mortgage); Scancio Motors, Inc. v. Subaru of New England, Inc., 555 F. Supp. 1121 (D.R.I. 1982) (dealership agreement).

10. *See, e.g.*, G. GUNTHER, *supra* note 3, at 540 (describing "hands off" approach to economic regulation).

11. 438 U.S. at 247.

12. 459 U.S. at 411.

regulation. Parts II and III examine this dispute, which has permeated Contract Clause decisions throughout the history of constitutional interpretation.

These two Contract Clause cases also differ in their formulation of constitutional doctrine. The *Allied Structural Steel* Court assumed its doctrinal test was intuitive and obvious,[13] while the *Energy Reserves* Court admitted that application of constitutional doctrine may appear arbitrary at times.[14] Part IV explores how these opinions shift rhetorical strategy when they reflect different judicial visions of economic life.

Allied Structural Steel and *Energy Reserves* depict a Supreme Court poised between two different visions of the state's role in regulating economic development. Judicial thought has reached an important historical crossroads. Every era of constitutional interpretation strikes its own balance between ensuring public ability to solve economic and social problems and, alternatively, preserving market incentives and personal choice by protecting private bargains against state impairment. These two recent Contract Clause decisions suggest that the Court is rethinking this fundamental balance for our era.

The constitutional structure of economic regulation can evolve in two ways from the present juncture. If *Allied Structural Steel* is an aberration, then the Constitution will continue to permit the government to take action in the public interest. On the other hand, if the contrasting *Energy Reserves* decision is limited to public utility regulation where redistributive arguments are strongest,[15] the *Allied Structural Steel* emphasis on protection of private bargains will become an important constitutional principle in limiting state power over economic affairs.

In sum, the *Allied Structural Steel* and *Energy Reserves* opinions are notable for three reasons. First, these decisions determine the standard of review for state economic regulation under the Contract Clause. Second, they illustrate the connection between judicial beliefs about markets and judicial use of language. Finally, these opinions denonstrate that a critical juncture between different judicial visions of economic life lies before the Supreme Court. The Court's choice between them, symbol-

13. *See infra* notes 168-71 and accompanying text.

14. *See infra* notes 172-73 and accompanying text.

15. Natural monopoly is the most common justification for public utility regulation. S. BREYER, REGULATION AND ITS REFORM 15 (1982). While natural gas suppliers, like the original plaintiff in *Energy Reserves*, are probably not natural monopolists, the defendant utility may well be. Redistribution in *Energy Reserves* was based on a legislative preference for consumers over producers in allocating a windfall between them. The same preference is applied when natural monopolists are subject to rate of return regulation. *See, e.g.*, S. BREYER, *supra*, at 19-20.

ized by the competing principles of *Allied Structural Steel* and *Energy Reserves*, will shape the nature of constitutional supervision of economic legislation.

I. Contrasting Rhetorical Strategies and Judicial Visions in Recent Contract Clause Cases

The *Energy Reserves* and *Allied Structural Steel* opinions differ in their attitude toward redistributive state legislation. The *Allied Structural Steel* Court invalidated a Minnesota law that aided those long-time employees of firms that closed their Minnesota plants before their pension plans had vested. The Court objected to the statute because it required employers to provide pension funds for those long-term employees not covered by a private plan even though the firms had never bargained for that liability. The Court held that redistributive legislation that infringes on private contracts violates the Constitution.[16]

In contrast, the *Energy Reserves* Court permitted the state of Kansas to impose a price ceiling on intrastate natural gas sold to a public utility following federal gas deregulation. This law restricted the windfall profits of the gas producer and benefited consumers by lowering electricity production costs and, consequently, electricity prices. The *Energy Reserves* Court explicitly endorsed legislative redistribution.[17]

Both opinions applied the Contract Clause analysis announced in the leading twentieth century Contract Clause decision, *Home Building Association v. Blaisdell*.[18] Under that test, the private right to security of a bargain is balanced against the public interest.[19] Five factors, largely

16. 438 U.S. at 250-51. This decision marked only the third time since 1940 that the Court invalidated state legislation under the Contract Clause. Wood v. Lovett, 313 U.S. 362 (1941), and United States Trust Co. v. New Jersey, 431 U.S. 1 (1977), were the previous Supreme Court cases. *United States Trust* held that laws impairing public contracts should be scrutinized carefully because of state self-dealing. *Accord* Troy Ltd. v. Renna, 727 F.2d 287, 294-96 (3d Cir. 1984) (higher Contract Clause scrutiny applies to public contracts than to private contracts); Don't Bankrupt Wash. Comm. v. Continental Ill. Nat'l Bank & Trust Co., 696 F.2d 692, 701 (9th Cir. 1983) (same); Peick v. Pension Benefit Guar. Corp., 724 F.2d 1247, 1264-65 (7th Cir. 1983) (federal self-dealing) (dictum); Sonoma County Org. of Pub. Employees v. County of Sonoma, 23 Cal. 3d 296, 591 P.2d 1, 152 Cal. Rptr. 903 (1979) (en banc). *Allied Structural Steel* applied the Contract Clause to a purely private contract, expanding the reach of the Contract Clause well beyond the holding in *United States Trust*. Although a regulated public utility, which might have been deemed a quasi-public entity, was a party to the agreement in *Energy Reserves*, the Court treated the contract as a purely private bargain because there was no suggestion of state self-dealing. 459 U.S. at 413 n.14.

17. 459 U.S. at 416-17 (deeming legitimate the state interest in protecting consumers from the escalation of natural gas prices).

18. 290 U.S. 398 (1934).

19. *Id.* at 445.

indicia of public purpose, test the constitutionality of the state's action. The legislation must: (1) serve a basic societal interest, not just benefit some favored group; (2) be tailored to fit the public purpose; (3) be justified by an emergency; (4) be limited to the duration of that emergency; and (5) be reasonable.[20]

Yet *Energy Reserves* and *Allied Structural Steel* differ markedly in how strictly they apply the *Blaisdell* factors. The *Allied Structural Steel* opinion considered all five factors and refined the test even further.[21] The *Energy Reserves* Court, in contrast, listed the factors in a footnote[22] and explicitly pointed out that emergency action is merely a factor in the decision and not a necessary requirement for upholding the state law.[23] The *Allied Structural Steel* Court undertook a formally structured balancing test. By devoting careful attention to each factor undercutting the state's claim of public interest, it indicated its intention to construe the public interest narrowly and to scrutinize economic regulation closely. The *Energy Reserves* Court adopted a casual rhetorical strategy, preferring to list the factors and announce its holding.

The difference between the rhetorical strategies adopted in these cases is examined below in part IV. Even without employing the conceptual tools of that later section, a rhetorical difference between the two decisions is apparent. This difference is encapsulated in the different levels of scrutiny utilized to review legislation challenged under the Contract Clause. The *Allied Structural Steel* majority required an intermediate level of scrutiny: state legislation must be "necessary to meet an important general social problem."[24] However, the *Energy Reserves* Court relaxed the level of scrutiny: state economic legislation must merely "have a significant and legitimate public purpose."[25]

There is also a fundamental inconsistency in the assumptions that both majorities make about market functions.[26] *Allied Structural Steel*

20. *Id.* at 444-47.

21. 438 U.S. at 242. *Allied Structural Steel* refined one factor, that the legislature advance a "basic" societal interest, into a requirement that the public interest justification be both "important" and "general." *See infra* text accompanying note 171.

22. 459 U.S. at 410 n.11.

23. *Id.* at 412; *cf. Allied Structural Steel*, 438 U.S. at 249 n.24 (emergency need not be of "great magnitude," suggesting by implication that a small emergency is necessary).

24. 438 U.S. at 247.

25. 459 U.S. at 411.

26. One commentator agrees that *Allied Structural Steel* allocates power between public and private sectors, Note, *Rediscovering the Contract Clause*, 97 HARV. L. REV. 1414, 1420 n.43, 1423-25, 1431 (1984), but argues that *Energy Reserves* is best explained by a concern with the allocation of power between legislative and judicial branches. *Id.* at 1426-29. Under this view, state laws must be prospective and general to keep the legislature from usurping the judicial function. Such an interpretation of legislative and judicial functions would form as

was predicated on an unstated assumption that the Minnesota labor market works well. Accordingly, the effect of a plant closing on the pension plan must have been bargained for and agreed to in each labor contract.[27] Only by this analysis does the contract reflect a personal choice that must be protected from legislative impairment. Assuming the labor market works well in Minnesota, there is no need for the remedial legislation struck down in *Allied Structural Steel*. If courts assume all markets work well, state legislatures must meet a heavy burden to justify regulatory and redistributive laws under the Constitution.

In contrast, the *Energy Reserves* decision reflected the Court's belief that the Kansas legislation remedied a genuine defect in the marketplace. Following deregulation, gas producers extracted extra profits by charging utilities higher prices unrelated to any increase in production costs.[28] The electric utility was forced to pay exorbitant prices to a gas producer due to a long-term contract with a price escalation clause that the parties had agreed to in an earlier year, assuming government price regulation would continue.[29] Although a spot market reallocated gas following the regulatory changes, transactions between producers and utilities were governed by contracts that did not provide for allocation of natural gas in the wake of deregulation. These transactions were not the product of market forces. Rather, they were the accidental by-product of language in contracts adopted in a specific regulatory environment. Prices did not reflect negotiated contingencies as they would in an unregulated market, but were governed by an unforeseen price-setting device. The contracts became an arbitrary mechanism that produced a windfall gain to sellers and an unforeseeable loss to buyers. When electricty prices rose as a consequence, the state legislature acted. Where courts expect such legislative responses, they test the constitutionality of the legislation at a low level of scrutiny.[30]

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radical a retrenchment as would a return to *Lochner* era views of the allocation of power between public and private sectors. In the modern era, where both branches of government must act to remedy market imperfections, judicial and legislative roles cannot be separated based on norms of prospectivity and generality. *See* Chayes, *The Role of the Judge in Public Law Litigation*, 89 HARV. L. REV. 1281 (1976). In any event, the view that the Contract Clause regulates politics and not economics is inconsistent with the main thread of Contract Clause jurisprudence outlined in part II of this Article. *See also infra* note 69.

27. See discussion of *Allied Structural Steel* in part III *infra*.

28. 459 U.S. at 415 (price rise prompted by demand shift).

29. *Id.*

30. *Cf.* United States v. Carolene Prods. Co., 304 U.S. 144, 152 (1938) (economic legislation constitutional as long as "it rests upon some rational basis within the knowledge and experience of the legislators"); J. HURST, LAW AND MARKETS IN UNITED STATES HISTORY 33 (1982) ("judges normally have given economic regulatory legislation the full benefit of a presumption of constitutionality").

Energy Reserves and *Allied Structural Steel*, although decided only five years apart, embody opposing attitudes toward redistribution. They apply the *Blaisdell* tests with different degrees of strictness.[31] They reflect inconsistent beliefs about the success of market allocations.[32] They use different rhetorical strategies to formulate Contract Clause analysis.[33] As will be seen, they represent different approaches to the constitutional interpretation of economic regulation.

II. Judicial Visions of Economic Life Shape the History of Contract Clause Adjudication

No fixed point of constitutional interpretation governs the balance between private rights and public needs. If the Supreme Court chose to alter this fundamental balance, it could change the structure of economic regulation in America. A Contract Clause case provides a vehicle for the Court to constitutionalize its view of appropriate government regulation. A comparison of leading Contract Clause cases of the nineteenth and twentieth centuries illustrates this point.

A. *Ogden v. Saunders*

Ogden v. Saunders,[34] an 1827 decision upholding the constitutionality of a New York prospective debtor relief law, is a landmark case on the subject of constitutional oversight of state economic regulation. The *Ogden* Court squarely faced the problem of accommodating both public interests and private rights. The Court's narrow majority[35] secured all existing contracts against interference from retrospective changes in state legislation, but preserved room for state action to alter prospective contracts.[36] In his dissent, Chief Justice Marshall argued for an impregnable wall around contracts to protect the private sphere from legislative interference. The different fears that motivated the majority and dissent in *Ogden* recur whenever the Court debates the constitutionality of economic regulation.

The *Ogden* majority feared adverse consequences if states were unable to act when confronted with economic emergencies. Justice Washington worried that with too much attention to private rights, "the

31. *See supra* text accompanying notes 24-25.

32. *See supra* text accompanying notes 26-30.

33. *See infra* notes 168-76 and accompanying text.

34. 25 U.S. (12 Wheat.) 213 (1827).

35. The Court split four to three, with Justices Washington, Johnson, Thompson, and Trimble in the majority. Justices Duvall and Story joined Chief Justice Marshall in dissent. This was the only major case in which Marshall dissented during his tenure on the Court.

36. *See infra* note 46 and accompanying text.

sphere of State legislation upon subjects connected with the contracts of individuals, would be abridged beyond what . . . States . . . would have consented to . . . ."[37] Justice Johnson insisted that "the rights of all must be held and enjoyed in subserviency to the good of the whole";[38] the public interest in justice and general welfare "must not be swallowed up and lost sight of while yielding attention to the claim of the creditor."[39] These Justices felt that strict application of the Contract Clause would paralyze states faced with social ills.[40] This is the same unhappy result modern writers accuse the *Lochner* era Court of fashioning.[41]

In direct contrast, dissenting Chief Justice Marshall opposed even prospective state bankruptcy laws because he feared state domination over personal autonomy absent strict Contract Clause enforcement.[42] In Marshall's view, debtor relief laws enacted by state legislatures under the Articles of Confederation had been "so alarming, as not only to impair commercial intercourse . . . but to sap the morals of the people, and destroy the sanctity of private faith."[43] Any reading of the Contract Clause that permitted "legislative interference with private rights"[44] would render this fundamental constitutional protection an "inanimate, inoperative, unmeaning clause."[45]

The majority and dissent also differed over the breadth of the protection afforded by the Contract Clause. Each side defined its perception of how future state actions could legitimately affect contracts. To the *Ogden* majority, state law at the time of contracting automatically formed a part of all contracts. Thus, all pre-existing contracts would be protected by the Contract Clause. The legislature remained free, however, to serve the public interest by limiting the scope of future contracts.[46]

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37. 25 U.S. at 258.

38. *Id.* at 282 (Johnson, J., concurring).

39. *Id.* at 283.

40. *Id.* at 283, 287 (Johnson, J., concurring), 319-20, 321-22 (Trimble, J., concurring).

41. *See, e.g.*, G.E. WHITE, THE AMERICAN JUDICIAL TRADITION 165-66 (1976) (*Lochner* era adoption of "liberty of contract" principle "jeopardized much of the welfare legislation of the early twentieth century").

42. 25 U.S. at 354-55 (Marshall, C.J., dissenting).

43. *Id.* at 355.

44. *Id.* at 336.

45. *Id.* at 339.

46. *Id.* at 260-61 (Washington, J.), 285 (Johnson, J., concurring), 297 (Thompson, J., concurring), 324 (Trimble, J., concurring). This distinction between prospective and retrospective state law still resonates for modern courts. *See, e.g.*, Railway Labor Executives' Ass'n v. Gibbons, 455 U.S. 457, 472-73 n.14 (1982) (dictum), and three cases striking retroactive laws: Fortune v. Naval Weapons Center Fed. Credit Union, 652 F.2d 842 (9th Cir. 1981); Garris v. Hanover Ins. Co., 630 F.2d 1001, 1004 (4th Cir. 1980); Wipperfurth v. U-Haul Co., 101 Wis.

Chief Justice Marshall argued that the majority's analysis would lead to state domination over private rights. He reasoned that if all contracts incorporate existing state law, then the state may circumvent Contract Clause protections merely by passing a law subjecting all future contracts to state modification at will.[47] The Chief Justice proved correct in this prediction. State constitutions and general incorporation laws routinely require corporate charters to include such provisions,[48] even though such charters are contracts between the state and private owners and hence are subject to Contract Clause protection.[49]

Marshall believed that state domination over private rights could be avoided only by declaring contractual rights independent of state law.[50] In this respect, his *Ogden* dissent restates two 1819 opinions that he wrote for the majority. *Sturges v. Crowninshield*[51] invalidated a retrospective New York bankruptcy law, and *Trustees of Dartmouth College v. Woodward*[52] prohibited a state from altering the structure of a state-chartered corporation to protect contractual expectations of the corporation's founding investors. Marshall would have permitted only those state laws that impaired the *remedy* for breach of contract, so long as the *right* to contract remained untouched.[53] For example, a state could abolish debtor's prison but could not release a person from any part of his debt.[54]

Although the *Ogden* majority feared state paralysis, it still left the balance between private rights and public interest skewed heavily in

2d 586, 304 N.W.2d 767 (1981); *cf.* Note, *A Procedural Approach to the Contract Clause*, 93 YALE L.J. 918 (1984) (proposing the prohibition of retroactive contractual impairments absent just compensation).

47. 25 U.S. at 339 (Marshall, C.J., dissenting). This argument had previously been made by Justice Story in Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 692 (1819). Story concurred with Marshall in *Ogden*.

48. L. FRIEDMAN, THE HISTORY OF AMERICAN LAW 125 (1973).

49. Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518 (1819); *cf.* M. HORWITZ, THE TRANSFORMATION OF AMERICAN LAW, 1780-1860, at 11-14 (1977) (early 19th century shift in view of corporations, from public to private entities).

50. 25 U.S. at 346-47, 350 (Marshall, C.J., dissenting).

51. 17 U.S. (4 Wheat.) 122 (1819). In *Sturges*, Marshall announced that the Contract Clause went well beyond prohibiting the state debtor relief laws that troubled the Constitution's Framers; it "establish[ed] a great principle, that contracts should be inviolable." *Id.* at 206.

52. 17 U.S. (4 Wheat.) 518 (1819). In *Dartmouth College*, Marshall declared that allowing the state to alter the terms of a corporate charter would convert the contractual protection of private rights into "a machine entirely subservient to the will of government." *Id.* at 653.

53. *Sturges*, 17 U.S. at 200.

54. *Id.* at 200-01.

favor of private rights.[55] While Marshall's right/remedy distinction and his use of the Contract Clause to preserve private rights against state legislation retained vitality throughout the nineteenth century, *Ogden* carved out a small sphere of legitimate public action, facilitating the Court's later expansion of state police power to promote economic development.[56]

B. *Home Building & Loan Association v. Blaisdell*

In *Home Building & Loan Association v. Blaisdell*,[57] the Supreme Court dramatically shifted the focus of Contract Clause doctrine and recognized the ability of state governments to act on behalf of the public interest regardless of private contracts. The fundamental debate in *Blaisdell* was reminiscent of *Ogden*, yet the Court reached a different result.

By the time *Blaisdell* was decided, the Contract Clause had lost much of its vitality, shrinking from "perhaps the strongest single constitutional check on state legislation during our early years as a nation"[58] to only a "minor" restraint.[59] States began to reserve the right to amend corporate charters in franchise grants, as Chief Justice Marshall had warned would occur in his *Ogden* dissent,[60] and to exercise their reserved police powers. As a result, the Contract Clause became less attractive to the Court as a doctrinal peg for restricting regulation. The *Lochner* era Court chose instead to constitutionalize its view of "the liberty of contract" through the Fourteenth Amendment Due Process Clause and

55. For decades after *Ogden*, until the general acceptance of the reserved powers doctrine as described *infra* note 56, the Contract Clause was interpreted as a strong check on state legislation. Hale, *The Supreme Court and the Contract Clause: I*, 57 HARV. L. REV. 512, 533 (1944) (after *Ogden*, ban on laws impairing obligations of pre-existing contracts absolute); Bronson v. Kinzie, 42 U.S. (1 How.) 311, 317-18 (1848) (state act affecting contract remedy impairs obligation of contract); Von Hoffman v. City of Quincy, 71 U.S. (4 Wall.) 535 (1866) (same).

56. The Supreme Court often relied upon the concept of unalienable reserve powers of states in mid-19th century Contract Clause decisions. *See, e.g.*, West River Bridge Co. v. Dix, 47 U.S. (6 How.) 507 (1848); Northwestern Fertilizing Co. v. Village of Hyde Park, 97 U.S. 659 (1878); Stone v. Mississippi, 101 U.S. 814, 821 (1879).

57. 290 U.S. 398 (1934). *Blaisdell* was decided three years before West Coast Hotel v. Parrish, 300 U.S. 379 (1937), which reached the same result by removing the substantive due process constraints on economic regulation that characterized the *Lochner* era. *But cf.* Nebbia v. New York, 291 U.S. 502 (1934) (limiting substantive due process restraints on police power) (decided two months after *Blaisdell*). *See generally* L. TRIBE, *supra* note 8, at 450 (end of *Lochner* era described).

58. *Allied Structural Steel*, 438 U.S. at 241.

59. G. GUNTHER, *supra* note 3, at 561; *see also* B. WRIGHT, THE CONTRACT CLAUSE OF THE CONSTITUTION 95 (1938); Hale, *The Supreme Court and the Contract Clause: III*, 57 HARV. L. REV. 852, 890-91 (1944).

60. *See supra* text accompanying notes 43-45.

avoid the Contract Clause.[61]

Blaisdell extended the constitutional scope of state police power beyond the traditional arena of health, safety, and morality to include laws regulating injurious business practices.[62] In *Blaisdell*, the Court upheld a Minnesota statute enacted during the Depression that postponed resale of foreclosed real estate and extended periods of redemption both retrospectively and prospectively. The *Blaisdell* majority attempted to harmonize the constitutional prohibition against the states' impairment of contractual obligation with the police power reserved to the states.[63] It raised the fear of state paralysis, discussed in *Ogden*, commenting that a state must "possess authority to safeguard the vital interests of its people."[64] Dissenting Justice Sutherland, motivated by the fear of state domination, deemed the *Blaisdell* decision one of the most momentous of his generation and accused the majority of failing to "see in it the potentiality of . . . ever-advancing encroachments upon the sanctity of private and public contracts."[65]

Blaisdell and *Ogden* both depict a Supreme Court wrestling with the appropriate role of state regulation in controlling business affairs. Although a century separates the decisions, the same fundamental dilemma is confronted in each. How should the Court balance private rights against public needs when interpreting the constitutionality of economic regulation?

A comparison of the recent *Allied Structural Steel* and *Energy Reserves* cases indicates that this dilemma continues to plague the Court. *Energy Reserves* followed *Blaisdell* by emphasizing that the Contract Clause "must be accommodated to the inherent police power of the State."[66] *Allied Structural Steel* focused on the "limits upon the power of the State . . . to abridge existing contractual relationships . . . ."[67] This ongoing dispute is not an academic exercise; its resolution determines the scope of public powers and the extent of property rights.

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61. B. WRIGHT, *supra* note 59, at 92, 95; Phillips, *The Life and Times of the Contract Clause*, 20 AM. BUS. L.J. 139, 148-55 (1982).

62. W. B. Worthen Co. v. Thomas, 292 U.S. 426, 432-34 (1934). The *Blaisdell* majority cited precedent for protecting injurious business practices using state reserved powers, but it largely appealed to public works cases. 290 U.S. at 437-39.

63. 290 U.S. at 435, 439; *cf. id.* at 442 (need to compromise individual rights and public welfare).

64. *Id.* at 434.

65. *Id.* at 448 (Sutherland, J., dissenting); *cf.* B. WRIGHT, *supra* note 59, at 99 (contemporary fear that *Blaisdell* gutted constitutional restrictions on legislative interference with contracts).

66. 459 U.S. at 410.

67. 438 U.S. at 243.

III. Private Rights and Perfect Markets: Revival of a *Lochner* Era Judicial Vision

A. Judicial Beliefs and Economic Regulation[68]

Two factors influence constitutional decisions structuring economic regulation: (1) a view of the appropriate balance between public and private spheres, and (2) a perception of the market's ability to allocate resources.[69] Courts may adopt either of two paradigm views about the first factor, the public/private dichotomy. Either individual rights are superior to state interests or state interests are superior to individual rights. Under the former view, property rights are never superseded by public concerns. This view conflicts with judicial decisions requiring redistribution of social resources no matter how pressing the public need. Under the latter view, private rights exist solely to promote social ends. For example, one might argue that private property exists to induce owners to care for the factors of production and to use them efficiently. But if a superior public interest arises, the state may legitimately abridge such property rights.

Courts may also adopt either of two paradigm views about the second factor, the success of market resource allocations. One view is that a

68. This section draws on Professor Henry Steiner's course, Law in the Regulatory and Welfare State, Harvard Law School, Spring 1981. In contrast to the view of this Article, Steiner argues that Depression-era shifts in legal view emphasizing the public, systematic, and group-oriented nature of law and social problems are irreversible, because they are connected with a fundamental technological change requiring large-scale economic organization.

69. This Article makes no attempt to delineate the class of laws concerned with economic regulation. While the Contract Clause, the Due Process Clause, and the Commerce Clause together regulate legislative action in the economic realm, the First Amendment governs laws regulating the market for ideas, and the Equal Protection and Due Process Clauses regulate legislative acts affecting the political process. *See* City of New Orleans v. Dukes, 427 U.S. 297 (1976) (Equal Protection Clause regulates the political process not the economic market); Eule, *Laying the Dormant Commerce Clause to Rest*, 91 YALE L.J. 425 (1982) (preferring political theory of Commerce Clause to economic theory). Some laws, like those limiting commercial speech, concern more than one of these realms. Therefore, they should be tested independently under the separate standard for each applicable constitutional clause.

Some recent commentators on the Contract Clause take the view that the Contract Clause is intended to prevent state legislators from acting in the interest of private groups rather than on behalf of the public good. Epstein, *Toward a Revitalization of the Contract Clause*, 51 U. CHI. L. REV. 703 (1984); Sunstein, *Naked Preferences and the Constitution*, 84 COLUM. L. REV. 1689, 1719-23 (1984); Wonnell, *Economic Due Process and the Preservation of Competition*, 11 HASTINGS CONST. L.Q. 91, 126-27 (1983). This argument attempts to extend the Contract Clause counter-revolution begun by *Allied Structural Steel* by applying the constitutional provision to remedy failures in the political process rather than failures with economic markets, a justification for this constitutional provision inconsistent with the main thread of Contract Clause jurisprudence. In any event, a showing that a challenged law does not impair the personal choice of contracting parties protects against the legislative factional bias these authors fear.

competitive free market ensures the proper allocation of resources. Alternatively, markets may be viewed as inherently imperfect, beset with economic problems like externalities and monopoly power.[70]

These beliefs comprise unarticulated judicial visions of economic regulation. When the Supreme Court risks state paralysis by interpreting the Constitution as favoring private economic freedoms, it stresses the sanctity of private rights and assumes that markets work perfectly. When the Court grants the public sphere priority in economic affairs, it decides that the public interest takes precedence over private rights and perceives markets as imperfect.

Shifts in judicial attitude toward the relative priority of private and public rights are exemplified in the evolution of two branches of law: (1) common law tort and contract principles and (2) the rise and fall of substantive due process analysis in constitutional adjudication.

1. Contract Law and Tort Law

The shifting jurisprudential balance between public and private spheres is evident in the evolution of tort and contract principles. In the mid-nineteenth century, courts viewed each contract as crystallizing the subjective will of its parties.[71] Implicitly, this view defined tort law as public policy ordering private affairs in situations where parties did not contractually provide for rights and obligations. Tort law was subservient to contract law since courts held private rights inviolate against the state.[72]

By the first quarter of the twentieth century, this conception of contract law had changed. Courts no longer restricted their task in contract cases to enforcing private bargains. Instead, they implemented social policy just as they did in cases involving tort law.[73] Under this twentieth century view, a judge would not enforce an express bargain if the public interest and social fairness required otherwise. For example, at the end

70. Externalities are social costs or benefits not borne by the parties to a market transaction. A. ATKINSON & J. STIGLITZ, LECTURES ON PUBLIC ECONOMICS 348-49 (1980) (externalities exemplify market failure). Monopoly power consists of a firm's ability to raise price by reducing output. R. POSNER, ANTITRUST LAW 8 (1980) (Chicago school of antitrust analysis adopts economists' definition of monopolies power). In a perfect market, neither externalities nor monopolies will exist.

71. For example, by 1825 a new doctrine of *caveat emptor* that strictly upheld the express bargain had replaced an 18th century "sound price" doctrine based on an earlier "equitable conception" of contract. M. HORWITZ, *supra* note 49, at 180.

72. *See* G. GILMORE, THE DEATH OF CONTRACT 62-66 (1974) (describing the 1932 debate between Corbin, representing the new view of contract law, and Williston, representing the older view, in drafting the Restatement of Contracts).

73. *See id.*

of the nineteenth century, notions of implied contracts such as implied warranties of fitness and merchantability cut back on the *caveat emptor* doctrine.[74] By the early twentieth century, courts imposed an implied warranty on manufacturers of consumer products regardless of privity of contract and independent of any express warranties made by the manufacturer to the dealer.[75] Tort law took precedence over contract law, and the intent of the parties became subservient to the needs of social policy.[76]

2. *Substantive Due Process*

The collapse of the *Lochner* substantive due process approach to economic regulation provides a concrete example of a shift in judicial vision. It demonstrates both a change in the relative priority of public and private spheres and a shift in the judicial view of the success of market resource allocations. The contrast between the Supreme Court's 1915 decision in *Coppage v. Kansas*[77] at the height of the *Lochner* era and its 1937 decision in *West Coast Hotel v. Parrish*,[78] which brought the *Lochner* era to a close, illustrates this shift.

In *Coppage*, the Court struck down a Kansas statute prohibiting "yellow dog" contracts.[79] The Court elevated private rights above state interests, holding that "[t]he mere restriction of liberty or of property rights cannot of itself be denominated 'public welfare,' and treated as a legitimate object of the police power . . . ."[80] In so deciding, the Court assumed that markets were perfect and concluded that any interference with the market necessarily interferes with the private sphere. It thus stated that "the liberty of making contracts does not include a liberty to procure employment . . . without a fair understanding,"[81] yet the worker is "free to decline"[82] employment on "yellow dog" terms, "just as the employer may decline to offer employment . . . [f]or . . . '[i]t takes two to make a bargain.' "[83] Economic class distinctions do not prove unequal bargaining power; they merely exhibit "those inequalities of for-

74. L. FRIEDMAN, *supra* note 48, at 473.

75. *See, e.g.*, MacPherson v. Buick Motor Co., 217 N.Y. 382, 111 N.E. 1050 (1916) (Cardozo, J.).

76. *See supra* note 73 and accompanying text.

77. 236 U.S. 1 (1915).

78. 300 U.S. 379 (1937).

79. "Yellow dog" was the name given to contracts in which employers required employees to agree not to join unions as a condition of employment.

80. 236 U.S. at 19.

81. *Id.* at 20.

82. *Id.* at 21.

83. *Id.*

tune that are the necessary result"[84] of the operation of free contract and private property.

In *West Coast Hotel*, the Court perceived both the law and the economy differently than it did in *Coppage* and thus found redistributive legislation constitutional. The *West Coast Hotel* decision upheld a Washington State minimum wage law for women and minors. The Court found private rights subservient to the public good; private liberty was "subject to the restraints . . . [of reasonable regulation] adopted in the interests of the community . . . ."[85] Hence, the Court held that "[t]his essential limitation of liberty in general governs freedom of contract in particular,"[86] and it validated redistributive legislation in the public interest. The Court justified minimum wage legislation by explaining, "[w]hat these workers lose in wages the taxpayers are called upon to pay. The bare cost of living must be met."[87] Thus, the Court saw the market as imperfect. It recognized "[t]he exploitation of a class of workers who are in an unequal position with respect to bargaining power and are thus relatively defenseless against the denial of a living wage."[88] The public good required this legislation because an imperfect market failed to protect women and minors.

B. The Revival of *Lochner* Beliefs in the 1970's: Renewed Judicial Faith in Markets and Sensitivity to Private Rights

By the time *West Coast Hotel* was decided, against the background of the Great Depression and the apparent inability of the market to improve economic conditions, the Supreme Court had adopted a belief in the priority of public rights and a vision of imperfect markets.[89] These beliefs, antithetical to *Lochner* era views, prevailed for a generation.[90] In the 1970's, however, the judiciary began to turn away from the view of superior public rights and favor the priority of private rights. This shift marked the first significant departure from the judicial vision of the 1930's.

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84. *Id.* at 17.

85. 300 U.S. at 391.

86. *Id.* at 392.

87. *Id.* at 399.

88. *Id.*

89. *See supra* text accompanying notes 85-88.

90. The Contract Clause did not form a significant barrier to state economic legislation between 1940 and 1960. *See, e.g.*, East N.Y. Sav. Bank v. Hahn, 326 U.S. 230 (1945) (upholding New York moratorium on mortgage foreclosures); City of El Paso v. Simmons, 379 U.S. 497 (1965) (discussed *infra* at text accompanying notes 136-40).

1. Reassertion of the Priority of Private Rights

In the 1970's the post-Depression judicial view that the public interest outweighed private rights came under successful attack. This shift reversed the positions of tort and contract law that had emerged early in the twentieth century.[91] Courts no longer automatically held contract law subservient to the social policies of tort law. A brief survey of Supreme Court cases decided under the "state action" doctrine demonstrates this change.

In the 1948 decision of *Shelley v. Kraemer*,[92] the state action doctrine reflected the priority of public rights. *Shelley* held that state enforcement of a racially restrictive covenant in a property contract constituted state action inconsistent with the principles of the Equal Protection Clause. The enforcement of private contracts was "no less attributable to government when embodied in common law than when expressed in statute or regulation."[93] Thus, the law of contracts reflected social policy.

By 1970 the Court began to limit the use of the state action doctrine to challenge private restrictions on property. In that year, the Court held that a public park limited to whites by the terms of a private testamentary trust would revest in the grantor's heirs rather than be converted to an integrated facility.[94] Enforcing the trustor's discriminatory intent was no longer state action, as it would have been under *Shelley*. Rather, the Court merely was giving a written instrument the interpretation intended by its maker. The Court held that the role of the state court was "to effectuate as nearly as possible the explicit terms of [the] will."[95]

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91. *See supra* notes 71-76 and accompanying text.

92. 334 U.S. 1 (1948).

93. L. TRIBE, *supra* note 8, at 694; *see also* Horwitz, *The History of the Public/Private Distinction,* 130 U. PA. L. REV. 1423, 1426 (1982).

94. Evans v. Abney, 396 U.S. 435 (1970).

95. *Id.* at 444. Later cases continued to reduce the scope of state action by viewing contract remedies as effectuating private rights rather than social policy. Adams v. Southern Cal. First Nat'l Bank, 492 F.2d 324 (9th Cir. 1973), *cert. denied*, 419 U.S. 1006 (1974) (California commercial code codification of common law contract rule allowing self-help repossession is not state action); Flagg Bros. Inc. v. Brooks, 436 U.S. 149 (1978) (remedy under New York Uniform Commercial Code is not state action); *see also* Brest, *State Action and Liberal Theory: A Case Note on* Flagg Brothers v. Brooks, 130 U. PA. L. REV. 1296 (1982) (*Flagg Bros.* inconsistent with view that contract law is social policy). Similarly, the Supreme Court has broadened the protection accorded private property rights against countervailing public interest claims under the public function test of state action. *Compare* Amalgamated Food Employees Local 590 v. Logan Valley Plaza, 391 U.S. 308 (1968) (protecting speech at private shopping center because of center's public function) *with* Hudgen's v. NLRB, 424 U.S. 507 (1976) (overruling *Logan Valley*). *See generally* Note, *Creditors' Remedies as State Action*, 89 YALE L.J. 538, 543 n.30 (1980) (discussing public function test).

In 1974, the Court confirmed its view of contract as private law in *Jackson v. Metropolitan Edison Co.*[96] The Court held that despite an extensive scheme of state regulation over a power company, the terms of a consumer's private contract with that company were not state action subject to due process analysis.[97] These later state action cases suggest that contract notions favoring private rights are reasserting their potent influence in areas previously dominated by tort principles.

2. *The New Market Vision of* Allied Structural Steel

To the extent judicial opinions now reflect an analysis tipped in favor of private rights over public interests, one of the two principles behind *Lochner* era decisions has returned to prominence. In the context of this conceptual shift, *Allied Structural Steel* is of tremendous importance because it provides the first evidence of a concomitant change in the other key principle, the judicial perception of how effectively markets allocate resources.[98] It is hard to overestimate the importance this second shift ultimately could have for the structure of economic regulation when viewed in conjunction with the recent renewal of judicial belief in the priority of private rights. A judicial counter-revolution may be in the making that could approach *Lochner* era extremes.[99]

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96. 419 U.S. 345 (1974).

97. *Id.* at 358; *cf.* Memphis Light, Gas & Water Div. v. Craft, 436 U.S. 1 (1978) (state ownership alters result in *Jackson*).

98. The view that markets work well has been advanced in the "law and economics" literature following the publication of Coase's article on the role of property rights in the opertion of markets. Coase, *The Problem of Social Cost,* 3 J.L. & ECON. 1 (1960); G.E. WHITE, TORT LAW IN AMERICA 218-19 (1980) (in contrast to earlier view that a market approach to defective products is inappropriate, 1970's torts scholarship assumes that when consumers have good information, the market can allocate risks sensibly); *cf.* RATIONAL EXPECTATIONS AND ECONOMETRIC PRACTICE (R. LUCAS, JR. & T. SARGENT ed. 1981) (modern macroeconomics has also produced a perfect markets theory challenging the imperfect markets view of Keynes and his followers). *But see* Horwitz, *Law and Economics: Science or Politics?*, 8 HOFSTRA L. REV. 905, 908 (1980) (conservatives seek "to use contractarian ideology to turn back the recent triumph of strict liabiity").

99. The *Lochner* era is known for its judicial activism in overruling legislation as well as for its judicial vision of private rights and perfect markets. *See, e.g.*, Community Communications Co. v. City of Boulder, 455 U.S. 40, 60 (1982) (Rehnquist, J., dissenting); L. FRIEDMAN, *supra* note 48, at 311. *But cf.* L. TRIBE, *supra* note 8, at 435 (idea of *Lochner* era hostility to legislation has been oversold). In terms of the analytic tools of this Article, periods of judicial activism and judicial restraint do not arise as independent ideological movements. Rather, judicial activism occurs when the courts disagree with the legislatures on the effectiveness of markets and on the priority of public or private interests. For example, the 1960's were characterized by judicial restraint in response to constitutional challenges to economic legislation, as both courts and legislatures believed that economic markets needed legislative intervention. However, at the same time the judicial branch was active in overruling racially restrictive legislation; courts believed that the political process and its legislative product did not adequately represent minorities, necessitating judicial intervention.

In *Allied Structural Steel*, the Supreme Court held that the Minnesota Private Pension Benefits Protection Act unconstitutionally impaired employment contracts. The Act imposed obligations on a company that the majority termed "conspicuously beyond those that it had voluntarily agreed to undertake."[100] The Act required employers to fund pensions for certain employees whose rights had not yet vested, in the event the employer terminated its Minnesota operations. The Court concluded that this requirement "compelled the employer to exceed bargained-for expectations and nullified an express term of [its own] pension plan."[101] Despite this conclusory language, the majority did not inquire whether the effect of a plant closing on the pension plan was actually considered during employment contract negotiations.

The *Allied Structural Steel* majority confirmed the recent trend toward acknowledging the priority of private rights over public needs. They focused on personal choice as the value protected by contract.[102] "Contracts enable individuals to order their personal and business affairs according to their particular needs and interests. Once arranged, those rights and obligations are binding under the law, and the parties are entitled to rely on them."[103] To find personal choice in the specific contract it protected, the *Allied Structural Steel* Court must have relied on an *implicit* faith in efficient market resource allocations. For, as the dissent pointed out, it is difficult to understand how the employer's obligations to workers in the event of a plant closing were chosen by either party to that agreement.[104]

The absence of *explicit* faith in market efficiency in the majority opinion can be detected by demonstrating how specific contractual provisions reflect the personal choice of the contracting parties. The fact that a contract allocates rights and duties between parties does not necessarily mean that party choice has been implemented. One of three additional circumstances must be found before it can be determined that parties chose the allocation of rights, duties, and resources of their contract. Personal choice is clearly manifested in the contract if the allocation of resources in the event of some contingency is *bargained over explicitly*.

100. 438 U.S. at 240.

101. *Id.* at 246 n.18.

102. This is the value which, according to liberal political theory, contract law protects. *See generally* C. FRIED, CONTRACT AS PROMISE 1-17 (1981).

103. 438 U.S. at 245; *cf* Phillips, *supra* note 61, at 176 (*Allied Structural Steel* signals judicial interest in protection of private rights).

104. 438 U.S. at 253 (Brennan, J., dissenting). Justice Brennan cited the fact that Allied did not consider the possibility of a plant's closing as an actuarial assumption in calculating its annual contributions to the pension plan as evidence that the contingency fell "outside the range of normal expectations of both the employer and the employee."

Personal choice also manifests itself in a second circumstance: when the contract's terms are applied in the event of a contingency that was *foreseen* by the parties at the time of contracting even if no explicit allocation for that event was made. Arguably, applying a contractual term also preserves party choice in a third circumstance: if the triggering event was *foreseeable* by the parties at the time of contracting, even absent evidence that the parties actually foresaw or explicitly bargained over the risk.[105]

The risk that triggered the Minnesota statute invalidated in *Allied Structural Steel*, a plant closing, does not fit any of these categories. The remedial Minnesota statute affected an employer's pension obligations only in the event that it closed a plant. This risk that Allied would be

105. Finding market failure forms a necessary prerequisite for legislative intervention to lead to efficient resource allocation. Market failure can occur in a decentralized system if the market does not allow firms, consumers, and workers to insure against every contingency. *See, e.g.*, Arrow, *The Role of Securities in the Optimal Allocation of Risk-Bearing*, 31 R. ECON. STUD. 91 (1964). Since transaction costs, imperfect information, and incentive problems prohibit the sale of third party insurance or the establishment of futures markets in most important contingencies, efficient resource allocation typically occurs only if the affected parties bargain at arm's length. For example, no one would insure a firm like Allied Structural Steel against the possibility that it would close a plant because that contingency is under the firm's complete control. Nor can the workers at any plant purchase third party insurance to hedge against that threat because the transaction costs of writing such a policy would be prohibitive. A market transaction insuring against the plant closing could only have occurred if it were bargained for by the parties. Thus, under an efficiency-based analysis of the Contract Clause, finding the absence of a bargain in the impaired contract justifies remedial legislation.

To improve economic efficiency, legislative intervention must also satisfy a second test. Even if the original contract did not take into account the possible occurrence of some later event, as long as (1) contract renegotiation is costless, and (2) the contract damage remedy gives parties the correct breach and reliance incentives, then renegotiation will lead to an efficient allocation of resources despite the occurrence of an unforeseen contingency. *See generally* A.M. POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 25-36 (1983). However, this second decentralized efficiency-producing mechanism is often absent because contract renegotiation following a contingency like a plant closing is costly—imagine the steel producer bargaining about pensions with laid-off workers. In sum, from an economic efficiency perspective, a state law altering contracts on account of a contingency improves resource allocation only if two often-found conditions hold: (1) markets do not work perfectly when contracts are written, and (2) markets work poorly when contracts are renegotiated.

Three important points about efficiency analysis deserve special note. First, state intervention to achieve a more efficient allocation— for example, reducing the costs of private renegotiations—may improve social resource allocation even if the legislature cannot achieve the "first best" allocation in every particular case. Thus, state laws need not be perfect to be successful. Second, only those efficient market resource allocations arrived at by bargaining manifest personal choice. *Ex post* reallocations, whether undertaken legislatively or through decentralized contract breach and renegotiation do not satisfy the liberal personal choice value grounding contract law. Therefore, the first prerequisite for an efficiency-producing legislative intervention is a sufficient test for proving absence of personal choice in private bargains. Finally, efficiency-based analysis takes no position on whether purely redistributive legislative transfers of wealth are socially beneficial.

forced to shut down was not allocated by the parties when each labor contract was made. It was surely not contemplated at the time the covered employees were hired.[106] It was probably not even foreseeable at that time.[107] Thus, the contract could not have reflected the personal choice of the steel firm or its employees in the event of a plant closing.

This inquiry into the *Allied Structural Steel* agreement shows that the allocation of rights and duties in the event of a plant closing cannot be considered the product of contract negotiations allocating that risk. Yet the Supreme Court assumed the contract embodied a bargain over party rights and duties in *all* events, including a plant closing.[108] The majority believed that Minnesota labor markets operated so well that each contract's operation in any imaginable future event—including a plant closing—was chosen by the parties. The Court's decision could be predicated only on a general faith in the success of market resource allocations.

In the latest major Contract Clause decision, *Energy Reserves*, the Court does not exhibit the same faith in markets as shown in *Allied Structural Steel*. In upholding a price ceiling on natural gas sales, *Energy Reserves* distinguished *Allied Structural Steel* on grounds that avoid a direct confrontation with the earlier Court's view of perfect markets. The Court stated that the law invalidated in *Allied Structural Steel* did not deal with an important social problem and was focused too narrowly to be in the public interest.[109] At the same time, the *Energy Reserves* Court accepted explicit legislative redistribution favoring consumers as a legitimate state goal, implicitly endorsing the priority of public needs over private property rights.[110] By narrowing the precedential effect of

106. *See supra* note 104.

107. The pension plan had been in operation at least a decade before the plant closed. 438 U.S. at 237, 246 n.18.

108. The majority referred to the company's reliance on its legitimate contractual expectations, 438 U.S. at 246, without investigating how the parties expected their agreement to apply in the event of a plant closing.

109. 459 U.S. at 412 n.13. The cases could also be distinguished by noting that the Court sustained state regulation of the industry with a history of regulation. *Compare Energy Reserves*, 459 U.S. at 413 *with Allied Structural Steel*, 438 U.S. at 249 (history of regulation differs). *See* Case Comment, *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 62 WASH. U.L.Q. 179, 188 (1984) (*Energy Reserves* deference to state legislation may be limited to laws affecting regulated industries). However, this distinction identifies doctrine with actual behavior, a logically unacceptable device. *See infra* note 175.

Since *Energy Reserves*, the Third Circuit has attempted to narrow the application of *Allied Structural Steel* on all conceivable grounds. In Troy Ltd. v. Renna, 727 F.2d 287, 299 (3d Cir. 1984), the *Allied Structural Steel* holding was limited to cases where (1) markets in fact work well so bargains reflect personal choice, (2) the state law does not address a broad social problem, and (3) the state is regulating a new area.

110. 459 U.S. at 416-17.

Allied Structural Steel and endorsing redistribution, the *Energy Reserves* Court signaled its view that markets may require remedial state action. In other words, the terms of private contracts need not always be applied as written.

Although *Energy Reserves* recognized that markets may not work well, the decision does not foreclose the Supreme Court from further elaboration of *Allied Structural Steel*. The Court could reaffirm its views of perfect markets and the priority of private rights in future Contract Clause cases by reading *Energy Reserves* narrowly, emphasizing that the parties to that particular contract anticipated that their agreement would incorporate future state price regulation because the industry was already heavily regulated.[111] The Court stated that the gas producer "knew its contractual rights were subject to alteration by state price regulation";[112] price regulation was "foreseeable as the type of law that would alter contract obligations."[113]

IV. Contract Clause Doctrine: A Connection Between Form and Substance

The conflict between *Allied Structural Steel* and *Energy Reserves* over the success of market allocations and the role of private rights centers on the doctrinal test of Contract Clause violation. Each opinion formulated that doctrine to reflect its own perception of the appropriate balance between public needs and private rights. This doctrinal dispute is a longstanding feature of constitutional history.[114] This section examines the rhetorical styles employed in the *Allied Structural Steel* and *Energy Reserves* opinions in light of their historical context.

A. Analytic and Conclusory Contract Clause Doctrine Before *Allied Structural Steel*

Both *Allied Structural Steel* and *Energy Reserves* formulate Contract Clause doctrine in terms of a *Blaisdell*-type balancing test. In the nineteenth century, Contract Clause doctrine normally was promulgated in terms of classification tests.[115] However, the difference in doctrinal style cuts across this distinction; it applies equally to balancing tests and classification tests. That difference lies in the Court's understanding of the role of its doctrinal test when applying the law.

111. *But see supra* note 109 (doubting the logical coherence of this distinction).
112. 459 U.S. at 416.
113. *Id.*
114. *See infra* text accompanying notes 115-40.
115. *See infra* text accompanying notes 119-24.

The test may be deemed "analytic" if it classifies legal and illegal activities. In a Contract Clause case a court must distinguish between legislation within the permissible public sphere and legislation that unconstitutionally impairs private rights. Analytic doctrinal tests are employed by courts that believe the distinction between constitutional and unconstitutional laws is intuitive and obvious.[116] Alternatively, courts that find these classifications difficult, arbitrary, or not apparent use reasoned judgment to apply what may be termed "conclusory" doctrinal tests.[117]

Historically Contract Clause opinions have used classification tests and balancing tests in both analytic and conclusory manners.[118] The discussion below surveys changing Contract Clause tests to highlight shifts in rhetorical style and points out the roots of the doctrinal dispute between *Allied Structural Steel* and *Energy Reserves*.

The *Ogden* dispute[119] involved competing analytic classifications. The majority proposed a prospective/retrospective test: only state laws that operate prospectively on contracts could satisfy the Contract Clause.[120] Chief Justice Marshall in dissent preferred a right/remedy distinction: state law may alter the remedy for breach of contract but may not infringe upon the right.[121] Both of these tests present "logical" classification schemes for detecting Contract Clause violations. The determination under either scheme is seen by its proponents as natural, intuitive and obvious; it is analytic.

Justice Washington used his *Ogden* opinion to point out a difficulty with Marshall's classification scheme. He believed Marshall's right/remedy scheme could be read to make all state legislation violative of the Contract Clause because courts would not admit the existence of cases difficult to classify, although no law merely alters the remedy without impairing the contractual right to some degree.[122] For example, if a state declares that no remedy exists for the breach of certain contracts, that statute necessarily limits the right to form such contracts. Justice Washington did not elevate this difficulty into a general critique of logical classification tests. His own prospective/retrospective distinction is prey

116. *See infra* notes 142-67 and accompanying text.

117. *Id.*

118. *Id.*

119. *See supra* text accompanying notes 34-56.

120. 25 U.S. (12 Wheat.) at 262 (Washington, J.), at 326 (Trimble, J., concurring).

121. *Id.* at 349-54 (Marshall, C.J., dissenting).

122. *Id.* at 261 (Washington, J.) (arguing that any limitation on the remedy for breach of contract necessarily limits the contractual right); *cf. id.* at 350 (Marshall, C.J., dissenting) (responding to this argument).

to a similar argument. A state law that attempts to forbid only future bankruptcy protections hurts those entrepreneurs who have already relied on the expectation of limited personal liability by suddenly raising the risks they had assumed and limiting their right to earn an anticipated future return. Such a law operates in part retroactively despite its intent.

Similarly, any attempt to classify state statutes into separate public and private spheres by logical distinctions founders. Either the test must be read to make all of the classified phenomena fill one of the spheres, or difficult cases make the classification scheme appear arbitrary and illogical. Despite this difficulty, such analytic tests seem intuitive and aesthetically satisfying to human minds,[123] and the analytic right/remedy distinction persisted in Contract Clause jurisprudence during the nineteenth century.[124]

By the latter half of the nineteenth century, the Supreme Court no longer accepted the right/remedy classification as intuitive. In 1867, in *Von Hoffman v. City of Quincy*,[125] the Court publicly expressed its doubts as to the "consistency and soundness"[126] of the distinction between right and remedy. *Hoffman* invalidated an Illinois statute limiting a city property tax that the city had previously pledged to secure bonds. The Court was intimidated by the authority favoring the old doctrine, a doctrine "supported by such an array of judicial names that it is hard for the mind not to feel constrained to believe they are correct."[127] The Court discussed an alternative doctrinal route to preserve private rights, but did not adopt this alternative.[128] It proposed only to view "direct" impairments of contracts as grounds for invalidating state law; indirect

123. *See generally* W.V. QUINE, *Natural Kinds*, in ONTOLOGICAL RELATIVITY AND OTHER ESSAYS 123 (1969) (fundamental linguistic classifications seem intuitive). Whether courts believe that mechanical application of doctrinal tests works successfully is a question of common perception. The referents of doctrinal legal tests are set by arbitrary social agreement rather than by logical analysis. Even an arbitrary classification can stick despite its logical problems. *Compare id. with* W.V. QUINE, *Two Dogmas of Empiricism*, in FROM A LOGICAL POINT OF VIEW 42-43 (2d ed. 1964) (the reference of individual terms or sentences is indeterminate) *and* H. PUTNAM, REASON, TRUTH AND HISTORY 33 (1981) (same). Hence, the broad outlines of any dichotomy employed in a constitutional doctrine will appear analytic to most observers, regardless of the arbitrariness in deciding any particular case. *But cf.* Kennedy, *The Stages of the Decline of the Public/Private Distinction*, 130 U. PA. L. REV. 1349, 1350 (1982) (once distinctions are exploded, analytic view can never be recaptured).

124. *See generally* B. WRIGHT, *supra* note 59, at 27-61.

125. 71 U.S. (4 Wall.) 535 (1867).

126. *Id.* at 554.

127. *Id.*

128. *Id.* at 553-54 (rejecting as contrary to precedent a Contract Clause construction that would prohibit only "direct" impairments while allowing legislation that affects contracts "incidentally" or "only by consequence").

burdens would be constitutional.[129]

The direct/indirect doctrine marked a new idea in the rhetoric of Contract Clause decisions. The Court suggested implicitly in *Hoffman* what it later admitted explicitly in 1880: "It is not always easy to tell on which side of the line which separates governmental from property rights a particular case is to be put . . . ."[130] Classification into public and private spheres no longer was understood as intuitive. The Court in *Hoffman* proposed a conclusory test to protect the core of the private sphere from infringement. This direct/indirect or "core and penumbra" approach to a classification test differed from the logical classification approach because it avoided complete domination by one sphere. A court employing it necessarily admits that some decisions must be arbitrary. The cores of the public and private spheres, however, cannot be sharply distinguished from each other just as the spheres themselves could not be distinguished in the earlier doctrine. Despite the *Hoffman* suggestion of analyzing doctrine in terms of inviolate core and less protected penumbra, nineteenth century Contract Clause doctrine never departed from the logical classification of spheres that characterized the Marshall era.[131] Perhaps this is because the general decline in use of the Contract Clause to invalidate state legislation gave little occasion for doctrinal elaboration.

In its 1934 *Blaisdell* decision the Supreme Court shifted from a classification test to a balancing test.[132] This shift was roughly concurrent with the introduction of balancing tests in other areas of the law.[133] The Depression era Supreme Court disowned both the right/remedy classification[134] and the direct/indirect distinction.[135] Classification tests of both the logical analytic variety and the conclusory/"core and penumbra" form were rejected in favor of judicial weighing and balancing of interests and equities.

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129. *Id.* at 553.

130. Stone v. Mississippi, 101 U.S. 814, 820-21 (1880) (upholding reserved police powers of the state).

131. *See, e.g., id.* at 821 (admitting difficulty of classification in principle, but not troubled by facts at issue).

132. *See supra* notes 57-65 and accompanying text. Justice Black preferred not to understand the *Blaisdell* doctrine as a balancing test so that he could cite it as precedent for his own preference for classification tests. El Paso v. Simmons, 379 U.S. 497, 524 (1965) (Black, J., dissenting). With its emphasis on harmonizing the reserved power with contractual rights, the doctrine is clearly a balancing test. *See supra* note 63 and accompanying text.

133. The Rule of Reason was read into antitrust law in Standard Oil Co. v. United States, 221 U.S. 1 (1911). Nuisance law also incorporated a balancing test in the early 20th century. M. HORWITZ, *supra* note 49, at 293 n.73 (citing a 1934 case).

134. W.B. Worthen Co. v. Kavanaugh, 295 U.S. 56, 60 (1935).

135. *Blaisdell*, 290 U.S. at 438.

Like classification tests, balancing tests may be applied in either a conclusory or analytic manner. If a court admits that some cases are difficult and require judgment, then it will apply an "unstructured," or conclusory, balancing test. Unstructured balancing is characteristic of twentieth century Contract Clause decisions.

An unstructured balancing test appeared in *City of El Paso v. Simmons*.[136] This 1965 Contract Clause case upheld the constitutionality of a Texas statute reducing the time period in which landowners could reinstate property forfeited for nonpayment of a debt owed the state. The *El Paso* Court admitted that applying the Contract Clause required judgment because of the interpenetration of public and private spheres.[137] The opinion made light of suggestions of invading the private sphere and gave great weight to evidence indicating public benefit from the challenged legislation. The Court described the act as "hardly burdensome"[138] to contracting parties "but nonetheless an important one to the State's interest."[139] This statement suggests an *ex post facto* justification for the Court's holding rather than a true analysis leading to that holding. The opinion simply concludes that "[t]he Contract Clause does not forbid such a measure."[140]

Alternatively, a court could apply a balancing test in a "structured" manner and analytically classify public and private spheres.[141] As discussed below, the Court came close to employing a structured balancing test in *Allied Structural Steel*, but reverted to an unstructured test in *Energy Reserves*.

B. Defining Property and Protecting Rights

The doctrinal formulation of the Contract Clause violation "test" aids in understanding *Allied Structural Steel* as a shift in the Supreme Court's view of markets. The Contract Clause doctrine set forth in *Allied Structural Steel* appears to reject conclusory balancing for an analytic test. This test is particularly associated with the vision of perfect markets that characterizes the substance of the opinion.

136. 379 U.S. 497 (1965).

137. *Id.* at 507.

138. *Id.* at 516-17.

139. *Id.*; *cf.* Exxon Corp. v. Eagerton, 103 S. Ct. 2296, 2304-07 (1983) (state statute prohibiting oil and gas producers from contracting to shift tax burden to customers does not impair private contracts).

140. 379 U.S. at 517.

141. *See* Henkin, *Infallibility Under Law: Constitutional Balancing*, 78 COLUM. L. REV. 1022, 1049 (1978) (proposing that courts "define and refine the weights" put into balance rather than engage in "ad hoc balancing").

There is a strong logical connection between a court's rhetorical style and its vision of market effectiveness. Markets work best when everything is tradeable, a situation that requires well-defined property rights. When a court intuitively defines property, it is likely to assume that markets work well and that classifying activities as public or private is obvious, intuitive, and analytic. But if a court must use reasoned judgment to define arbitrary property lines, it will have difficulty separating public and private realms. Hence, it will employ a conclusory doctrine to separate spheres. The court will question whether property with indeterminate boundaries can be traded and therefore will view markets as imperfect.[142]

Two Contract Clause cases decided a century apart illustrate the link between rhetorical style and markets vision. In both cases, the Supreme Court addressed centrally, although not expressly, this fundamental problem of defining, or "bounding," property. In *Charles River Bridge v. Warren Bridge*,[143] decided in 1837, the Court interpreted a state franchise for a toll bridge as nonexclusive. Although the majority did not claim the state had a reserved power to grant a competing franchise, it held that the original grant must be construed as nonexclusive absent express indication from the legislature.[144]

In the view of the Justices deciding *Charles River Bridge*, an exclusive franchise was a well-defined concept.[145] Defining the extent of the nonexclusive franchise for the purpose of determining when beneficial competition becomes unacceptable trespass, or when competition becomes illegitimate taking if promoted by state grant, constituted a stickier issue. Thus, the majority in *Charles River Bridge* used reasoned judgment to define the extent of the nonexclusive franchise and employed conclusory doctrine to separate private and public spheres. This point is made succinctly by Justice McLean, concurring with the opinion of the Court: "The right granted to the Charles River Bridge Company, is, . . . to a certain extent, exclusive; but to measure this extent, presents the chief difficulty."[146] McLean argued that the franchise extended a

142. *Cf.* Kennedy, *Form and Substance in Private Law Adjudication*, 89 HARV. L. REV. 1685, 1738-41 (1976) (proposing "rhetorical analogy" between style and substance). One might read Kennedy's individualism/altruism dichotomy as stating this Article's state paralysis/state domination poles in connotatively favorable form. If so, the present discussion refines Kennedy's theoretical argument by identifying the perfect or imperfect market vision aspect of that dichotomy as providing the crucial link with rhetorical form.

143. 36 U.S. (11 Pet.) 420 (1837).

144. *Id.* at 548-49 (Taney, C.J.).

145. *See, e.g., id.* at 560 (McLean, J., concurring) (exclusive franchise is as well-defined as a tract of land).

146. *Id.*

"reasonable distance" above and below the physical timbers of the original bridge. The distance "must not be so great as to subject the public to serious inconvenience, nor so limited as to authorize a ruinous competition."[147] He chose a conclusory test to measure impairment of the bridge franchisè because of the less bounded nature of the property right that defined the private sphere.

In contrast, dissenting Justice Story had no difficulty defining the property right as an exclusive franchise. He asked "what limits can be assigned to such a franchise? The answer is obvious . . . ."[148] By diverting traffic, a new bridge "would be a nuisance to the old bridge, [and] would be within the reach of its exclusive right."[149] Story used an analytic test because the property limits appeared obvious to him, and land-based nuisance law applied intuitively. "There is nothing new in such expositions of incorporeal rights," he concluded.[150]

Modern economics associates competition with perfect markets and monopoly with imperfect markets. This association, however, is misleading for understanding the market view held by early nineteenth century Justices. Story required an exclusive franchise to support his view that markets work well. The recipient of the original franchise made a fair bargain with the legislature to assume the risks of development in exchange for a right to the proceeds. No private party would have accepted a franchise qualified by nonexclusive right. Story asked rhetorically, what legislature "would ever have dreamed of such a qualification of its own grant . . . when it sought to enlist private capital and private patronage to insure the accomplishment of it?"[151]

The majority's preference for a nonexclusive franchise betrayed its view that markets required state action to remedy market failure. If such state franchises were deemed exclusive, an inefficient spectacle would occur. One would "soon find the old turnpike corporations awakening from their sleep, and calling upon this Court to put down the improvements which have taken their place."[152] Story's well-defined conception of property boundaries connected an analytic classification of public and private spheres with a perfect market vision. But when the majority

147. *Id.* at 564. McLean measured infringement of the original franchise by the loss in value in its toll receipts, not by its physical distance from the competing bridge. *Id.* at 565.

148. *Id.* at 614 (Story, J., dissenting).

149. *Id.*

150. *Id.*

151. *Id.* at 615. In modern terms this market system of bidding for an exclusive right would be called competition "for the field." *See, e.g.*, Demsetz, *Why Regulate Utilities?*, 11 J.L. & ECON. 55 (1968).

152. 36 U.S. at 552-53.

viewed property as not well-defined or lacking specific boundaries, a conclusory classification of spheres accompanied an imperfect market vision.

Two consequences of the *Charles River Bridge* majority view that unassisted markets typically did not work well illustrate the practical importance of judicial vision. First, because the state intervened to remedy market failure, the reserved police powers doctrine that flourished later in the nineteenth century is a direct descendant of the *Charles River Bridge* holding.[153] Second, government-promoted competition remedied the market imperfection in *Charles River Bridge*; thus, since 1837, competition rather than monopoly has promoted American economic development.[154]

A century later the Court again implicitly faced the problem of defining incorporeal property in *Home Building & Loan Association v. Blaisdell*.[155] *Blaisdell* extended the reserved powers of the state to cover the regulation of injurious business practices.[156] In determining the scope of the mortgagee's (creditor's) rights that were free from state intervention, the Court defined the creditor's property right. The majority explained that the core of the mortgage right was not infringed by extending the period of redemption. The obligation for interest and the right to obtain a deficiency judgment remained. Only the penumbra of the right was affected. "Aside from the extension of time, the other conditions of redemption are unaltered."[157] Like the holding in *Charles River Bridge*, this reasoning required judgment; the lines drawn were not intuitive.

The *Blaisdell* dissent considered the bounds of the property right to be obvious, not dependent on any judgment of reasonableness. "[W]hether the statute operated directly upon the contract or indirectly by modifying the remedy, its effect was to extend the period of redemption. That this brought about a substantial change in the terms of the contract reasonably cannot be denied."[158]

Motivated by an imperfect market vision and an inability to define property easily, the *Blaisdell* majority adopted a conclusory, unstructured balancing test to separate private and public spheres. The dissent,

153. J. HURST, LAW AND MARKETS IN UNITED STATES HISTORY 84-85 (1982) (citing *Charles River Bridge*, 36 U.S. at 547).

154. M. HORWITZ, *supra* note 49, at 130-39. Antitrust laws that promote development by competition rather than monopoly have philosophical roots in this case.

155. 290 U.S. 398 (1934).

156. *See supra* text accompanying notes 57-65.

157. 290 U.S. at 425 (Hughes, C.J.); *cf. id.* at 438 (obligation/remedy distinction is one of "reasonableness").

158. *Id.* at 480 (Sutherland, J., dissenting).

believing it knew the bounds of the property right, would have used a logical classification between right and remedy,[159] defending the perfect market vision of the *Lochner* era.

The connection between economic vision and rhetorical style aids in understanding the history of Contract Clause cases. The main thread of nineteenth century Contract Clause doctrine employed analytic classification schemes such as the right/remedy or prospective/retrospective distinctions, concurrent with a perfect market vision.[160] Only toward the end of the century did a direct/indirect test emerge.[161] The emergence of this test coincided with the rise of the large corporation and its market power and with the development of the reserved powers doctrine, which gave legislatures the tools to remedy market failure.[162] This conclusory classification test demonstrated that the Court had difficulty separating private and public spheres. It viewed markets as imperfect; thus it had trouble defining the limits of property.[163] The *Lochner* era Supreme Court then returned to a perfect market view, protecting "the liberty of contract" from state infringement.[164] In the Great Depression judges once again switched, viewing markets as imperfect and overthrowing *Lochner*.[165] Conclusory, unstructured balancing tests therefore characterize later twentieth century Contract Clause cases.[166]

As is shown below, *Allied Structural Steel* partially returned to an analytic test by structuring a balancing test to determine Contract Clause violations. The structure of the doctrine in that case confirmed the Court's conclusion that markets work well. Since *Allied Structural Steel*, courts have relied on an analytic distinction between the retrospective and prospective effects of state statutes in Contract Clause cases.[167] They have adopted a logical classification, *Ogden*-type test even though the retrospective holding in *Blaisdell* should have foreclosed this option.

Energy Reserves halted the trend toward a structured Contract Clause balancing test. By returning to a conclusory balancing test and

159. *Id.*

160. *See generally supra* notes 36-56 and accompanying text.

161. *See supra* notes 129-31 and accompanying text.

162. A. CHANDLER, JR., THE VISIBLE HAND 285 (1977) (modern industrial enterprise, integrating mass production with mass distribution, grew "to dominate many of the nation's most vital industries" between 1880 and 1910); *see supra* notes 47-56 and accompanying text.

163. *Cf.* International News Serv. v. Associated Press, 248 U.S. 215, 248-67 (1918) (Brandeis, J., dissenting) (incorporeal property is difficult to define, but judicial restraint considerations made judicial remedy for market failure inadvisable).

164. *See supra* notes 8, 99 and accompanying text.

165. *See supra* text accompanying notes 77-88.

166. *See supra* text accompanying notes 136-40.

167. *See supra* note 46.

endorsing legislative redistribution, the opinion suggested that the Court has had second thoughts about its recent perfect market vision. Within only five years, the Supreme Court has taken opposite views on the fundamental issue of market effectiveness, indicating this shift by changing its rhetorical style.

C. Differing Rhetorical Strategies in *Allied Structural Steel* and *Energy Reserves*

Allied Structural Steel retreated from an unstructured balancing test in three respects, suggesting that the distinction between public and private spheres is logical and intuitive rather than arbitrary. First, the *Allied Structural Steel* Court applied the balancing test as if it were a per se rule: if the contractual impairment is minimal, sufficient public purpose to justify the legislation under the Constitution can be presumed.[168] Second, the *Allied Structural Steel* Court clarified the *Blaisdell* balance by specifically applying each element.[169] The careful articulation of public interest factors in *Allied Structural Steel*'s analysis stands in stark contrast to the almost totally hidden balance in *El Paso*.[170] Finally, the *Allied Structural Steel* Court refines the analysis of the individual balancing factors into small-scale logical classification tests. For example, the Court transforms the "basic" societal interest required by *Blaisdell* into one that is both "important" and "general."[171] The Court implied that each factor could be determined by intuitive logic and then weighted to yield an analytic conclusion about Contract Clause violation.[172] This feature of the *Allied Structural Steel* doctrine, a more structured balancing test, is dispensed with in *Energy Reserves* where the public interest must be "significant" and "legitimate."[173] These are conclusory terms rather than small-scale logical classification tests.

If the *Allied Structural Steel* Court intended to create a balancing test which could be used to determine analytically Contract Clause violations, it only moved part way toward its goal. The per se nature of its

168. 438 U.S. at 245 n.17 (dictum). This per se rule has frequently been used to dismiss cases since *Allied Structural Steel*. *See, e.g.*, Insurer's Action Council v. Markman, 653 F.2d 344 (8th Cir. 1981); Morseburg v. Balyon, 621 F.2d 972 (9th Cir. 1980); Rowell v. Harleysville Mut. Ins. Co., 272 S.C. 108, 250 S.E.2d 111 (1978), *overruled*, 294 S.E. 2d 336, 340 (1982).

169. 438 U.S. at 242, 247-50.

170. *See supra* text accompanying notes 136-40.

171. 438 U.S. at 247. *But cf.* United States Trust Co. v. New Jersey, 431 U.S. 1, 19 n.17 (1977) (remedy/obligation distinction treated as rule of thumb rather than as analytic test).

172. By selectively quoting language from *El Paso*, described *supra* at text accompanying notes 136-40, the *Allied Structural Steel* majority reinterpreted that example of unstructured balancing as if it were analytic. 438 U.S. at 243 n.14.

173. 459 U.S. at 411.

doctrinal test appeared only as dictum since the challenged statute was found unconstitutional. The majority did not explain which indicia of public purpose would be most convincing, leaving the weight of each factor unknown. Furthermore, characterizing the Minnesota legislation as narrow in focus is controversial, unlike intuitive classification schemes. Nevertheless, in *Allied Structural Steel* the Supreme Court came closer to adopting the *Ogden* analytic doctrinal test of Contract Clause violation than it has come at any time since the Great Depression.

A rhetorical device as old as *Ogden* utilizes a circular and incoherent reliance on the disruption of actual expectations to determine contractual impairment. The device does not prevent a court from invoking its judicial vision. Rather, it merely obscures the theory on which the decision is based. The *Allied Structural Steel* majority employed this device when it tested contractual impairment by the cost of disrupting settled expectations.[174] However, the device could not entirely hide that Court's view of market efficiency. Indeed, the logical incoherence of this rhetorical device requires a court eventually to fashion doctrine in other terms.

The circularity of this "actual expectations" doctrine obscures judicial vision and manifests itself in a logical paradox. Actual expectations embodied in any contract surely include background state law. Parties may economize on contract drafting by relying on state law to fill in the legal gaps. If any contract incorporates the whole body of background state law, government cannot change any law without infringing some party's background expectations; state paralysis results. On the other hand, if a court declares that all agreements are subject to later alteration at the will of the state legislature, no party to any contract can ever claim that settled expectations were harmed by a change in state law; state domination results. Also, the efficiency gained by relying on background state law dissipates because contracting parties no longer can be sure that standard gap-filling provisions will be applied in the future. Since the *Allied Structural Steel* Court would not allow Minnesota to alter its regulation of pension plans, it could not make such a declaration. The Court's application of the actual expectations view in *Allied Structural Steel* pushed toward state paralysis, consistent with the Court's perfect markets vision.[175]

174. *See, e.g.*, 438 U.S. at 247 ("unexpected liability in potentially disabling amounts").

175. This dilemma over expectations is escaped by recognizing that the purpose of Contract Clause doctrine is to notify contracting parties of legitimate state law expectations. Conditioning the doctrine on actual expectations creates circular logic; the doctrine becomes indeterminate. This circularity is unavoidable whenever doctrine is identified with actual expectations, including expectations based on that doctrine, or with actual behavior, including

The *Energy Reserves* Court returned to an unstructured test, avoiding a refined analysis of contractual impairment. Rather than applying individually the five *Blaisdell* indicia of public purpose to the state legislation, as was done in *Allied Structural Steel*, the *Energy Reserves* Court announced what it deemed to be the public policy behind the Kansas Act. It simply reasoned in a conclusory manner that "there can be little doubt about the legitimate public purpose behind the Act."[176]

Conclusion

Even if the trend toward critical use of the Contract Clause begun in *Allied Structural Steel* continues, the Supreme Court will not immediately dismantle the welfare state and require a return to the unregulated competition of the *Lochner* era. However, the underlying vision of effective markets suggested in that case, combined with the view that private rights have priority over the public interest, leads ultimately to state paralysis in the face of pressing public concerns.

If *Energy Reserves* successfully aborts that trend, the severe economic recession of the early 1980's deserves part of the credit. Hard times help dispel any faith that markets work well.[177] Whichever view gains a majority now, the perfect market and private rights vision of *Allied Structural Steel* or the imperfect market and public interest vision of *Energy Reserves* will dominate the constitutional structure of economic regulation for the next generation, and so determine the agenda of American economic life.

Energy Reserves and *Allied Structural Steel* represent an ongoing battle for the mind of a still undecided Supreme Court. The *Allied Struc-*

behavior modified in light of that doctrine. *Cf.* Perry v. Sinderman, 408 U.S. 593 (1972) (procedural due process doctrine based on behavior). To avoid circularity, Contract Clause doctrine must define the value protected by contracts independent of any particular agreement. L. TRIBE, *supra* note 8, at 465, 467 n.11. In the long run, which is the appropriate horizon for interpreting a document that aims at shaping society, constitutional clauses must be read to incorporate fundamental natural rights, as Justice Marshall attempted in his *Ogden* dissent. *See* 25 U.S. (12 Wheat.) at 345-46. (Marshall, C.J., dissenting). *But cf.* Brest, *The Fundamental Rights Controversy: The Essential Contradictions of Normative Constitutional Scholarship*, 90 YALE L.J. 1063 (1981) (fundamental rights interpretation of Constitution incapable of resolving tension between majority rule and minority rights). Within liberal social theory, protection of personal choice is the right the Contract Clause protects, as that is the value supported by contract law. *See supra* note 102. *Cf.* Exxon Corp. v. Eagerton, 103 S. Ct. 2296, 2305-06 (1983) (private parties cannot be allowed to evade state power over private rights by making a contract about those rights).

176. 459 U.S. at 417.

177. To the extent that material conditions create a climate that shapes ideas, the economic emergency of the 1930's led to the *Blaisdell* decision upholding redistributive economic legislation. This law almost certainly would have been held unconstitutional in the 19th century.

tural Steel vision would, if taken to its logical conclusion, return constitutional supervision of economic regulation to a strict scrutiny last seen in the *Lochner* era. Yet *Energy Reserves* casts doubt on whether the Supreme Court has altered its market vision in the generation since *Blaisdell*; to the extent *Allied Structural Steel* is now seen as an anomoly, the change in judicial vision is stillborn and the Contract Clause counterrevolution halted.