# The Contract Clause: A Return to the Original Understanding*

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## Introduction

The Contract Clause provides: "No State shall . . . pass any . . . Law impairing the Obligation of Contracts."[1] As one of the few prohibitions the Framers of the Constitution imposed on the states, and one of a handful of prohibitions that relate to the rights of private individuals rather than the prerogatives of the federal government,[2] the Clause was clearly of significance to the Framers. In the first sixty years under the Constitution, the Clause was often litigated and was given an interpreta-

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1. U.S. CONST. art. I, § 10, cl. 1.

2. Section 10 of Article I catalogues these prohibitions:

> [1.] No State shall enter into any Treaty, Alliance, or Confederation; grant Letters of Marque and Reprisal; coin Money; emit Bills of Credit; make any Thing but gold and silver Coin a Tender in Payment of Debts; pass any Bill of Attainder, ex post facto Law, or Law impairing the Obligation of Contracts, or grant any Title of Nobility.
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> [2.] No State shall, without the Consent of the Congress, lay any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing its inspection Laws: and the net Produce of all Duties and Imposts, laid by any State on Imports or Exports, shall be for the Use of the Treasury of the United States; and all such Laws shall be subject to the Revision and Control of the Congress.
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> [3.] No State shall, without the Consent of Congress, lay any Duty of Tonnage, keep Troops, or Ships of War in time of Peace, enter into any Agreement or Compact with another State, or with a foreign Power, or engage in War, unless actually invaded, or in such imminent Danger as will not admit of delay.

tion of significant scope. By the midpoint of this century, however, the Clause was construed so narrowly that it became little more than a historical curiosity. Although the Supreme Court has revived the Clause somewhat in recent years, it has not restored it to its original importance.

Correctly interpreted, the Contract Clause prohibits all retrospective, redistributive legislation which violates vested contractual rights by transferring all or part of the benefit of a bargain from one contracting party to another.[3] This interpretation is supported on several grounds. First, the interpretation has very substantial support in the history of the Clause at the Constitutional Convention and the ratifying conventions in the several states. Second, this construction of the Clause can be applied in a neutral manner that requires a minimal amount of judicial balancing of interests.[4] Third, and most fundamentally, the interpretation of the Contract Clause as a prohibition against retrospective interference with contracts comports with the ideal of government that the Framers actually possessed: namely, a government constrained by a concept of the rule of law, restrained in circumstances which present particular risks of majoritarian disregard for minority rights, and rendered stable by barriers against abrupt change in social policy and organization.

The early period of contract clause jurisprudence was largely faithful to this original understanding of the Clause. Since then, the Clause has fallen into desuetude. Misinterpreted as a form of substantive economic due process, the Clause was wrongly discredited when that doctrine was rightly discarded. The Court's recent jurisprudence concerning the Contract Clause represents a step in the direction of the original understanding, but it leaves the Framers' intent unfulfilled, because the scrutiny applied to state retrospective legislation is too lenient and the objects of the Court's protection are too limited. In arguing for a return to the original understanding of the Contract Clause, we anticipate and respond to concerns that the current, narrow interpretation of the Clause is necessary to permit the operation of the modern regulatory and welfare state. We also question Professor Richard Epstein's well-crafted, but

3. A specific intent to redistribute resources between the parties is not a prerequisite to a contract clause violation. If the natural consequence of the legislation is to redistribute resources between contracting parties, the legislation is at odds with the Contract Clause. For a discussion of examples of legislation which illustrates this point, see *infra* text accompanying notes 132-135.

4. *See* Note, *A Procedural Approach to the Contract Clause*, 93 YALE L.J. 918 (1984) [hereinafter Note, *A Procedural Approach*] (arguing that a balancing approach to the Contract Clause is undesirable because it "creates uncertainty in the law and undermines the integrity of the legal system"). The author of this Note also argues that the Contract Clause prohibits all retrospective impairments of contracts.

ahistorical argument in favor of giving the Clause even broader scope through application to prospective as well as retrospective laws.

## I. Understanding the Contract Clause: The Rule of Law, Factionalism, and Political Stability

John Locke's *Second Treatise on Civil Government*,[5] the primer on just government at the time of the Nation's founding, makes clear that the rule of law was a presupposition of liberty in a civil society. For Locke, as for many modern theorists of the rule of law,[6] liberty in a civil society is the ability to live "within the Allowance of [the] Laws."[7] However, to conform to the law one must be able to know it; one cannot know what does not exist. Therefore, when Locke speaks of law in civil society he speaks of "settled standing Laws."[8] No man would yield his liberty to civil society if an arbitrary will could apply laws retrospectively to conduct that conformed to the law at the time it was undertaken.[9] The task of the Framers was to translate this basic postulate of just government into rules of practical application by which governing power could be restrained from departing from "settled standing Laws" and injuring interests which were created in reliance on such laws. Such practical laws obviously had to be framed with a view to protecting the most significant interests from such situations in which arbitrary will would most likely be exercised.

It is not surprising, therefore, that the rule of law is a concept that animates the entire Constitution. The prohibitions against bills of attainder, and ex post facto laws,[10] and takings of property without just compensation,[11] are all derived from strands of the concept of the rule of law: laws must be general, prospective, and relatively stable.[12] The Contract Clause, like the Ex Post Facto Clause, is particularly concerned with the

5. J. LOCKE, SECOND TREATISE ON CIVIL GOVERNMENT 324 (Laslett ed. 1980) (emphasis omitted).

6. *See, e.g.*, Raz, *The Rule of Law and Its Virtues*, in LIBERTY AND THE RULE OF LAW 6-7 (R. Cunningham ed. 1979).

7. J. LOCKE, *supra* note 5, at 324.

8. *Id.* at 377.

9. In Locke's words:

> Absolute Arbitrary Power, or Governing without *settled standing Laws*, can neither of them consist with the ends of Society and Government, which Men would not quit the freedom of the state of Nature for, and tie themselves up under, were it not to preserve the Lives Liberties and Fortunes; and by *stated Rules* of Right and Property to secure their Peace and Quiet.

*Id.* (emphasis in original).

10. U.S. CONST. art. I, §§ 9-10.

11. U.S. CONST. amend. V.

12. This formulation of the rule of law is taken from Raz, *supra* note 6, at 6-7.

requirement of prospectivity. Prospectivity is an essential requirement of the rule of law because only prospective laws allow citizens to plan their conduct so as to conform to the law.[13]

The requirement that legislation be prospective is easier stated than applied. As the Framers knew, a generalized prohibition against all retrospective rules might render the legislature powerless. Almost all laws operate retrospectively in that they must defeat the subjective expectations of those who planned their conduct according to the existing law.[14] Therefore, in implementing the requirement of prospectivity, the Framers had to choose a few fundamental contexts in which to afford citizens a safe harbor from retrospective legislation while preserving the legislative function. The Framers chose contractual rights and liberty from criminal sanctions. Importantly, by stating the prohibition against retroactive legislation in terms of a tangible interest, like a vested contract, the Framers established a set of fairly narrow principles capable of judicial application.[15]

While the Framers did not believe that representative government inevitably led to legislation that oppressed minority rights in violation of the rule of law, they were concerned that factions, isolated and bereft of allies, would be oppressed. In *The Federalist No. 10*, Madison argued that in large republics such oppression is unlikely, because the diversity of factions will counterbalance one another.[16] Significantly, however, Madison believed that the prohibition against violation of contracts should apply to state governments, because such small republics would not likely have sufficient diversity of faction to prevent oppression.[17] In terms of the Madisonian understanding of factions, one can readily understand why those with vested and beneficial contractual rights might be isolated. Those who stand to benefit from contract are identifiable,

13. Professor Hayek has summarized this view as a requirement that government act through "rules which make it possible to foresee with fair certainty how the authority will use its coercive powers in given circumstances and to plan one's individual affairs on the basis of this knowledge." F. HAYEK, THE ROAD TO SERFDOM 72 (rev. ed. 1976) (quoted in Note, *Rediscovering the Contract Clause*, 97 HARV. L. REV. 1414, 1426 (1984) [hereinafter Note, *Rediscovering the Contract Clause*]).

14. *See infra* note 31.

15. One rationale for the Contract Clause may be related to the theory of separation of powers. It is the province of the legislature to announce prospective law; it is the province of the judiciary to declare the rights under existing law. *See* Fletcher v. Peck, 10 U.S. (6 Cranch) 87, 136 (1810) ("It is the peculiar province of the legislature to prescribe general rules for the government of society, the application of those rules to individuals in society would seem to be the duty of [the judiciary].").

16. THE FEDERALIST NO. 10, at 61-62 (J. Madison) (Modern Library ed. 1961).

17. *See* Letter of James Madison to Thomas Jefferson (Oct. 24, 1787), *reprinted in* 1 P. KURLAND & R. LERNER, THE FOUNDERS' CONSTITUTION 646-47 (1986).

and those who are obligated by contract have an obvious interest in avoiding their obligations. Moreover, any loss from legislation impairing such existing contractual obligations would be borne entirely by those who benefit from them.[18] In short, legislation redistributing resources between parties to a contract by voiding obligations presents a particular danger of oppression to a minority interest or faction.

The interpretation of the Contract Clause as a prohibition against retrospective interference also comports with the Framers' deep interest in promoting stability, even at the expense of immediate implementation of the popular will. Because they believed that republican government would be endangered if policies were susceptible to change by impassioned and momentary majorities, the Framers created barriers to protect social stability against such change.[19] Thus, even if the Contract Clause retards democratic change by forcing legislatures to defer policy changes until current contractual obligations are satisfied, the delay is wholly consistent with the Framers' general desire to temper abrupt changes in social policy, however popular, in the interest of stability.

## II. The Origins of the Contract Clause

What is known of the origins of the Contract Clause supports the proposition that the Clause is intended to prohibit retrospective legislation interfering with contractual rights. The actual proposal for a Contract Clause was made at the Constitutional Convention on August 28, 1787 by Rufus King. To a section already prohibiting bills of attainder and ex post facto laws, King moved to add a provision prohibiting interference with contracts "in the words used by the Ordinance of Cong[ress] establishing new States."[20] This statement strongly suggests that the

18. In contrast, prospective economic legislation has a more diffuse effect and therefore those most adversely affected by it will likely have a significant number of natural allies in the political process. *See infra* note 141 and accompanying text.

19. For instance, in order to prevent rapid changes in policy, the Framers instituted six year terms for members of the Senate. *See, e.g.*, THE FEDERALIST NO. 62, at 406 (J. Madison) (Modern Library ed. 1961). In justifying the creation of the Senate, Madison catalogued the dangers of "mutable policy":

> The internal effects of a mutable policy are still more calamitous. It poisons the blessings of liberty itself. It will be of little avail to the people, that the laws are made by men of their own choice, if the laws be so voluminous that they cannot be read, or so incoherent that they cannot be understood; if they be repealed or revised before they are promulgated, or undergo such incessant changes that no man, who knows what the law is today, can guess what it will be to-morrow. Law is defined to be a rule of action; but how can that be a rule, which is little known, and less fixed?

*Id.*

20. Madison reports King's remarks as follows: "Mr. King moved to add, in the words used in the Ordinance of Cong[ress] establishing new states a prohibition on the States to interfere in private contracts." 2 J. MADISON, THE RECORDS OF THE FEDERAL CONVEN-

Contract Clause was modeled on this ordinance—the Ordinance of the Northwest Territory[21]—which Congress had established under the authority of the Articles of Confederation just six weeks before. The relevant clause in the Ordinance provided:

> And in the just preservation of rights and property, it is understood and declared, that no law ought ever to be made, or have force in the said territory, that shall in any manner whatever interfere with, or affect private contracts, or engagements, bona fide, and without fraud previously formed.[22]

The phrasing makes clear that this Clause was designed to prohibit the states of the Northwest Territory from interfering with vested property and contract rights through the passage of retrospective laws. This interpretation is confirmed by the placement of the Clause directly after a clause that prohibited the taking of property or services without compensation.[23] Laws taking property are obviously retrospective laws, because they abrogate rights possessed by property owners under prior positive law.

Governor Morris of Pennsylvania immediately objected to King's proposal on the grounds that it interfered with majoritarian rule in the states.[24] Madison acknowledged the "inconvenience" that would be caused by the frustration of majority will "but thought on the whole it would be overbalanced by the utility of it."[25] Madison's journals do not

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TION 439 (M. Farrand ed. 1911). King's express limitation of the clause to private contracts seems to have disappeared at some point because the version of the clause that emerged from the Constitutional Convention did not make any distinction between public and private contracts. In Fletcher v. Peck, 10 U.S. (6 Cranch) 87 (1810), the first significant decision applying the Contract Clause, Chief Justice Marshall held that public contracts also came within the ambit of the Clause. For a full discussion of the debates at the Convention relating to the Contract Clause, see B. WRIGHT, THE CONTRACT CLAUSE AND THE CONSTITUTION 1-12 (1938).

21. An Ordinance for the Government of the Territory of the United States North-West of the River Ohio, 1 Stat. 51 (1789).

22. *Id.*

23. This Clause provided in full: "[A]nd should the public exigencies make it necessary, for the common preservation, to take any person's property, or to demand his particular services, full compensation shall be made for the same." *Id.*

24. Madison reports Morris' remarks as follows:

> This would be going too far. There are a thousand laws relating to bringing actions—limitations of actions which affect contracts—The Judicial power of the U.S. will be a protection in cases within their jurisdiction; and *within the State itself a majority must rule, whatever may be the mischief done among themselves.*

J. MADISON, *supra* note 20, at 439 (emphasis added).

25. In full, Madison remembered his statement as follows:

> Mr. Madison admitted that inconveniences might arise from such a prohibition but thought on the whole it would be overbalanced by the utility of it. He conceived however that a negative on the State laws could alone secure the effect. Evasions might and would be devised by the ingenuity of the Legislatures . . . .

specify what he saw as the purpose of the Clause; however, the Northwest Ordinance to which King referred in introducing the contract clause provision presents a clear purpose—namely, "the just preservation of the rights and property" from retrospective legislation.[26] After Madison's remark, Colonel Mason of Virginia, soon to be an ardent anti-federalist, renewed the kind of objections expressed by Governor Morris, saying that "cases will happen that cannot be foreseen, where some kind of interference will be [proper and essential]."[27] James Wilson of Pennsylvania responded to these objections by noting that the proposal prohibited "retrospective interferences only."[28]

After this exchange, a motion forbidding states from passing "bills of Attainder or retrospective laws" was introduced and passed. By this wording, the convention delegates sought to expand the previous prohibition against retrospective criminal laws—which had been accomplished by the prohibition against ex post facto laws—to all laws, criminal and civil.[29] However, the Committee on Style changed the Clause to read,

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*Id.* at 440.

26. *Id.* at 439.

27. In full, Colonel Mason stated: "This is carrying the restraint too far. Cases will happen that can not be foreseen, where some kind of interference will be proper, & essential—He mentioned the case of limiting the period for bringing actions on open account. . . ." *Id.*

28. *Id.* Madison queried: "Is not that already done by the prohibition of ex post facto laws, which will oblige the Judges to declare such interferences null and void." *Id.* The answer to Madison's query was suggested on August 29, 1787 by Dickinson who read from Blackstone to prove that this prohibition applied only to criminal legislation. *Id.* at 448.

29. Some have argued that the Ex Post Facto Clause was intended to prohibit retrospective civil laws as well as retrospective criminal laws. *See, e.g.*, 1 W. CROSSKEY, POLITICS AND THE CONSTITUTION IN THE HISTORY OF THE UNITED STATES 324-51 (1953). If this interpretation were correct, the Contract Clause would have to be given prospective effect, or it would be rendered superfluous. The Court's seminal decision in Calder v. Bull, 3 U.S. (3 Dall.) 386 (1798), squarely rejected this view of the Ex Post Facto Clause. Moreover, the two state constitutions that were written before the Federal Constitution and use the term ex post facto to make it clear that the prohibition against ex post facto laws in American constitutionalism referred to criminal laws. *See* North Carolina Declaration of Rights § 24 (1776), *reprinted in* 5 F. THORPE, THE FEDERAL AND STATE CONSTITUTIONS: COLONIAL CHARTERS, AND OTHER ORGANIC LAWS OF THE STATES, TERRITORIES, AND COLONIES NOW OR HERETOFORE FORMING THE UNITED STATES OF AMERICA 2788 (1909) ("That retrospective laws, punishing facts committed before the existence of such laws, and by them only declared criminal, are oppressive, unjust, and incompatible with liberty; wherefore no *ex post facto* law ought to be made."); Maryland Declaration of Rights § 15 (1776), *reprinted in* 3 F. THORPE, *supra*, at 1688 (same wording of clause). When New Hampshire wanted to prohibit all retrospective laws, criminal and civil, it eschewed the phrase ex post facto and used the general phrase "retrospective." *See* New Hampshire Constitution § 23 (1784), *reprinted in* 4 F. THORPE, *supra*, at 2456 ("Retrospective laws are highly injurious, oppressive and unjust. No such laws, therefore, should be made, either for decision of civil causes, or the punishment of offences."). Moreover, *The Federalist Papers* also reflect an understanding that the Ex Post Facto Clause was a protection against the operation of criminal law. *See* THE FEDERALIST NO. 84, at 577 (A. Hamilton) (Modern Library ed. 1961).

"No state shall pass any bill of attainder, nor ex post facto laws, nor laws altering or impairing the obligation of contracts," and subsequently deleted the predicate "altering."[30] Because of these changes the Clause closely resembled a shortened version of the language from the Northwest Ordinance referenced by King.[31]

The Contract Clause did not occasion much debate in the ratification process, but what debate there was confirms that the purpose of the clause was to prohibit retrospective legislation interfering with contractual rights. In the one extended discussion of the Clause in *The Federalist*, Madison emphasized that the Clause was designed to prevent property rights from being displaced by legislation "contrary to the first principles of the social compact and to every principle of sound legislation."[32] Madison specifically linked the Clause to the prohibition against ex post facto laws, which again suggests that the "first principles" he mentioned were those required by a concept of the rule of law, similar to Locke's, which held that property rights and liberty interests could be dissolved only by prospective laws of general applicability.

The one extended discussion of the Contract Clause from those opposed to the ratification of the Constitution emphasized its an-

30. The present wording provides: "No State shall . . . pass any . . . Law impairing the Obligation of Contracts." U.S. CONST. art. I, § 10, cl. 1.

31. We can only speculate at the reason for the Committee's changes but, as suggested earlier, one difficulty in a prohibition against all retrospective laws is its breadth. Almost all laws operate retrospectively in that they may defeat the expectations of those who planned conduct with respect to existing laws. By casting the prohibition against retrospective laws in terms of the specific matters of criminal prosecution—the Ex Post Facto Clause—and interferences with pre-existing contractual rights—the Contract Clause—the Framers created provisions capable of judicial application.

32. Madison's full discussion was as follows:

> Bills of attainder, *ex post facto* laws, and laws impairing the obligation of contracts, are contrary to the first principles of the social compact, and to every principle of sound legislation. The two former are expressly prohibited by the declarations prefixed to some of the State constitutions, and all of them are prohibited by the spirit and scope of these fundamental charters. Our own experience has taught us, nevertheless, that additional fences against these dangers ought not to be omitted. Very properly, therefore, have the convention added this constitutional bulwark in favor of personal security and private rights; and I am much deceived if they have not, in so doing, as faithfully consulted the genuine sentiments as the undoubted interests of their constituents. The sober people of America are weary of the fluctuating policy which has directed the public councils. They have seen with regret and indignation that sudden changes and legislative interferences, in cases affecting personal rights, become jobs in the hands of enterprising and influential speculators, and snares to the more-industrious and less-informed part of the community. They have seen, too, that one legislative interference is but the first link of a long chain of repetitions, every subsequent interference being naturally produced by the effects of the preceding. They very rightly infer, therefore, that some thorough reform is wanting, which will banish speculations on public measures, inspire a general prudence and industry, and give a regular course to the business of society.

THE FEDERALIST NO. 44, at 291 (J. Madison) (Modern Library ed. 1961).

timajoritarian nature and the concerns noted by those who opposed the Clause at the Convention.[33] Luther Martin complained that the Clause would prevent the states from passing legislation in times of crisis. He particularly objected to the Clause's implicit prohibition of debtor relief legislation, common at the time, that either prevented courts from enforcing foreclosures or authorized courts to defer payments. Such relief legislation, Martin argued, was necessary to prevent "*monied* [men] from *totally* destroying the *poor* though even *industrious* debtor."[34]

Some have contended that Martin's remarks demonstrate that the Contract Clause was aimed solely or principally at state debtor relief legislation.[35] State debtor relief legislation, to be sure, was passed during the economically troubled period between the end of the Revolution and the framing of the Constitution.[36] Therefore, there is little doubt that such legislation was one of the major evils that the Clause was designed to eradicate.

The Clause, however, is framed in general terms and nowhere mentions debtor relief legislation. Moreover, the debtor relief theory of the Clause has little support from the history of the Convention or ratifica-

33. *See supra* notes 24-28 and accompanying text.

34. Mr. Martin's discussion of the Contract Clause was as follows:

> I considered, Sir, that there might be times of such *great public calamities* and *distress*, and of such *extreme scarcity* of *specie* as should render it the *duty* of a government, for the *preservation* of even the *most valuable part* of its citizens in some measure to interfere in their favour, by passing laws *totally* or *partially stopping* the courts of justice, or authorizing the debtor to pay by *installments*, or by delivering up his property to his creditors at a *reasonable* and *honest* valuation. The times have been such as to render regulations of this kind necessary in most, or all of the States, to prevent the *wealthy creditor* and the *monied man* from *totally* destroying the *poor* though even *industrious* debtor - - *Such times* may *again* arrive. I therefore voted against depriving the States of this power, a power which I am decided they ought to possess, but which I admit ought only to be exercised on very important and urgent occasions. I apprehend, Sir, the principal cause of complaint among the people at large is, the public and private debt with which they are oppressed, and which, in the present scarcity of cash, threatens them with destruction, unless they can obtain so much indulgence in point of time that by industry and frugality they may extricate themselves.

Martin, *Information to the General Assembly of the State of Maryland*, (1788), *reprinted in* 2 THE COMPLETE ANTI-FEDERALIST 4.64-.65 (H. Storing ed. 1981) (emphasis in original).

35. Adherents of this theory generally argue that the prohibition is closely related to the constitutional prohibition against the states' maintenance of their own currency and simply represents an attempt by the Framers to protect a national free market from restrictions imposed by the states. As a recent commentator has stated, "[t]he economic nationalism approach portrays the Contract Clause as a limitation on the states' power to attack economic powers on the national level." Note, *Rediscovering the Contract Clause*, *supra* note 13, at 1421. *See* 1 W. CROSSKEY, *supra* note 29, at 352-60.

36. For a discussion of legislation favoring debtors, see J. FISKE, THE CRITICAL PERIOD OF AMERICAN HISTORY 193-96, 204-09 (1899). For a survey of such legislation, see A. NEVINS, THE AMERICAN STATES AFTER THE REVOLUTION, 1775-1789 at 457, 523, 537, 549, 570-71 (1924).

tion proceedings. At the Convention, the Clause was modeled on a provision in the Northwest Ordinance intended to protect property and contract rights from the kind of retrospective legislation which the Framers believed was contrary to the rule of law.[37] Moreover, in *The Federalist*, Madison viewed the Clause as a "bulwark in favor of . . . private rights" against improper legislation generally.[38] Thus, the history of the Clause suggests that it was aimed at all retrospective, redistributive schemes in violation of vested contractual rights, of which debtor relief was merely a prime example.

## III. The History of the Contract Clause in the Supreme Court

The history of the Contract Clause in the Supreme Court can be divided into four periods. In the first period, which lasted through the late 1880's, the Supreme Court vigorously applied the Clause to strike down state legislation that retrospectively impaired or altered contractual rights, whether these rights were held against other private individuals or against the state itself.

In the second period, which began after the Civil War and lasted until the 1930's, the Contract Clause largely fell into disuse. The rise of substantive due process enabled proponents of *laissez-faire* to argue successfully for the invalidation of *prospective* as well as *retrospective* economic legislation, thereby rendering the Contract Clause largely superfluous.

In the third period, which began in 1934 with the Court's decision in *Home Building & Loan Association v. Blaisdell*,[39] the standard of review for substantive due process analysis continued to be applied to cases under the Contract Clause. However, as the due process standard became very relaxed, the Contract Clause was rendered a virtual nullity.

In the final period, the modern Court has undertaken to revive the Clause to a limited extent and has subjected to greater scrutiny a state's retrospective interference with core contractual expectations. These recent decisions, however, have not been informed by a coherent jurisprudence and by no means have restored the Clause to its original importance.

37. *See supra* notes 21-23 and accompanying text.
38. THE FEDERALIST No. 44, at 291 (J. Madison) (Modern Library ed. 1961).
39. 290 U.S. 398 (1934).

### A. The Early Decisions

For the first eighty years, the Contract Clause appears to have generated more Supreme Court cases than any other constitutional provision—reflecting the original importance of the Clause.[40] The first significant Supreme Court opinion interpreting the Contract Clause was *Fletcher v. Peck*.[41] The case reflected three broad themes of contract clause analysis in the Marshall Court: (1) the application of the Clause to public as well as private contracts; (2) the broad construction of the term "contract" in the Clause; and (3) the near absolute prohibition of impairments of contracts.

The issue in *Fletcher* was whether the Georgia Legislature could revoke a land grant made by a previous legislature. Chief Justice Marshall relied generally on the text of the Constitution to defend the proposition that the Contract Clause applied to contracts between the state and a private party as well as to contracts between private parties. He asserted that the words of the Contract Clause are "general, and are applicable to contracts of every description."[42] Second, in deciding that the land grant was a contract, Marshall reasoned simply that "[a] grant is a contract executed, and it creates also an implied *executory* contract, which is, that the grantee shall continue to enjoy the thing granted according to the terms of the grant."[43] Finally, the Court viewed the Clause's prohibition as virtually absolute. Those seeking to support the abrogation of the grant argued that revocation was justified because the grant had been tainted with fraud, but this argument proved unavailing.[44]

In 1819, the Court had the opportunity to continue its broad construction of the Clause in two cases: *Sturges v. Crowninshield*[45] and *Dartmouth College v. Woodward*.[46] In *Sturges*, the Court invalidated a New York bankruptcy law which discharged a debt owing on a contract

40. For a comprehensive discussion of all contract clause cases decided in the Supreme Court under Chief Justices Marshall and Taney, see B. WRIGHT, *supra* note 20, at 51-88.

41. 10 U.S. (6 Cranch) 87 (1810).

42. *Id.* at 137.

43. *Id.* at 123.

44. *Id.* at 133-34. Another characteristic of early contract clause jurisprudence was its tendency to vacillate between an analysis which was narrowly premised upon the text of the Constitution and a mode of analysis based on the less determinant contours of natural law. Although Marshall relied on the Contract Clause in *Fletcher*, he also speculated that the legislation might be invalid because of natural law: "It may well be doubted whether the nature of society and of government does not prescribe some limits to the legislative power; and, if any be prescribed, where are they to be found, if the property of an individual, fairly and honestly acquired, may be seized without compensation." *Id.* at 135.

45. 17 U.S. (4 Wheat.) 122 (1819).

46. 17 U.S. (4 Wheat.) 518 (1819).

made before the law was passed. First, the Court rejected the creditor's claim that New York lacked the power to pass any bankruptcy laws because Congress' power over bankruptcy was exclusive.[47] The Court then held that the Contract Clause rendered the statute unconstitutional as applied to debts incurred before its passage.[48] In rejecting the contention that the Clause was merely intended to prevent laws that permitted debtors to pay their previous debts in installments, Chief Justice Marshall again emphasized the general language of the Clause:

> No men would use terms embracing a whole class of laws, for the purpose of designating a single individual of that class. No Court can be justified in restricting such comprehensive words to a particular mischief to which no allusion is made. . . . The Convention appears to have intended to establish a great principle, that contracts should be inviolable.[49]

The *Sturges* Court ignored arguments that the Clause should not apply to statutes which had a legitimate state purpose—in this case relief for the poor from the oppression of debts. In modern terminology, retrospective debtor relief was *not* justified by the state's interest in promoting the general welfare.[50] The Court's decision in this respect was supported not only by the absolute language of the Clause but also by the history surrounding its inclusion in the Constitution. As discussed above,[51] the Clause was passed against the background of the debtor relief legislation that sought to advance, by abrogating contractual rights, what was per-

47. 17 U.S. (4 Wheat.) at 196.

48. *Id.* at 199, 207. Until its decision in *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398 (1934), the Court continued to invalidate almost all debtor relief statutes that operated on debts incurred before their passage, whether these statutes took the form of preventing a creditor from selling assets at prices lower than assessed value, or of providing the debtor with more time to redeem property seized for debt. *See* Howard v. Bugbee, 65 U.S. (24 How.) 461 (1860) (invalidating Alabama statute that authorized a judgment creditor of a mortgagor to redeem the property on paying the purchase price, the interest, and charges for a two year period after the foreclosure sale); Bronson v. Kinzie, 42 U.S. (1 How.) 311 (1843) (invalidating law that provided that no judicial sales should be made unless two-thirds of the appraised value was bid for property).

The Court did, however, sustain statutes liberating debtors from prison, even if their debts were incurred before the passage of the statute. *See* Mason v. Haile, 25 U.S. (12 Wheat.) 370, 378 (1827) ("Such laws act merely upon the remedy and that in part only. They do not take away the entire remedy, but only so far as imprisonment forms a part of the remedy."). The Court's doctrine that a change in remedies was not necessarily an impairment did not greatly circumscribe the Contract Clause, for the Court was vigilant in striking down any scheme that directly delayed or reduced payment to the creditor, even if it could be characterized as a remedy.

49. 17 U.S. (4 Wheat.) at 205-06.

50. Hunter, the attorney for the debtor, argued to no avail that the statute be upheld in light of the states' "natural, inherent, and indispensable power, of discharging poverty, distress, and absolute indigence and inability, from payment." *Id.* at 156.

51. *See supra* notes 33-36 and accompanying text.

ceived to be the general welfare. Moreover, Luther Martin had specifically argued that the Clause interfered with the majority's ability to promote the general welfare by protecting the rich against the poor. Yet the Contract Clause was included in the Constitution in the face of such objections.

In the second case, *Dartmouth College v. Woodward*,[52] the issue was whether New Hampshire had violated the Contract Clause by enacting legislation that: (1) changed the College's charter to increase the Board of Trustees from twelve to twenty-one members; (2) vested power of appointment of the new members in the governor; and (3) provided for a Board of Overseers with veto power over the acts of the Trustees. The Court first addressed the question of whether the Charter was a contract. Chief Justice Marshall answered in the affirmative, reasoning that property had been conveyed for a charitable purpose in exchange for the Charter.[53] To the argument that the Framers did not contemplate the use of the Clause in such a situation, Marshall responded:

> It is not enough to say, that this particular case was not in the mind of the Convention when the article was framed, nor of the American people, when it was adopted. It is necessary to go farther and to say that, had this particular case been suggested, the language would have been so varied, as to exclude it, or it would have been made a special exception.[54]

Chief Justice Marshall also rejected the argument of counsel that the contract was not impaired, because the number of Trustees appointed according to its original terms remained unchanged and the legislature had merely added additional terms to the Charter, including a provision for additional Trustees.[55] Marshall interpreted the word "impair" in the Contract Clause as equivalent to "alter."[56]

Marshall's only defeat in arguing for a broad protection of contracts was in *Ogden v. Saunders*.[57] In *Ogden*, the Court held that states may enact laws affecting contracts so long as these laws operate prospectively. Marshall argued that the right to contract is a natural right protected by the Contract Clause; therefore, any law that interferes with the right to contract, whether it operates prospectively or retrospectively,[58] violates

52. 17 U.S. (4 Wheat.) 518 (1819).

53. *Id.* at 631-650.

54. *Id.* at 644.

55. *Id.* at 603, 610.

56. *Id.* at 651 ("By this contract the crown was bound, and could have made no violent alteration in its essential terms, without impairing its obligation.").

57. 25 U.S. (12 Wheat.) 213 (1827).

58. *See id.* at 346-47. Marshall declared that "individuals do not derive from government their right to contract, but bring that right with them into society. . . ." Therefore for Mar-

the Clause. The majority, however, held that the Clause refers to contractual obligations as they were created through the operation of positive law at the time of the contract. Under this view, only laws that retrospectively alter obligations incurred under prior law would violate the Clause.[59] In support of their argument, the Justices in the majority relied on the original intent of the Clause as it is implicit in the structure of the Constitution. Justice Johnson contended that by classing together bills of attainder, ex post facto laws, and laws impairing the obligation of contracts, the Framers made clear that they were creating a "general provision against arbitrary and tyrannical legislation over *existing* rights, whether of person or property."[60] Thus, an appeal to the original understanding of the Clause as an affirmation of the rule of law was crucial in limiting its scope. In *Ogden,* the Court correctly saw the Clause as a protection against retrospective legislation only, and ultimately rejected the natural rights construction of the Clause that might have ushered in substantive due process years before the *Lochner* era.[61]

This first period of Contract Clause interpretation was largely faithful to the intent of the Clause. The Marshall Court correctly resisted the argument that a Clause framed in general terms should only be applied to particular kinds of debtor relief legislation. The Court was also right to interpret the word "impair" as the equivalent of "alter" in view of the purpose of the Clause: a contract can be impaired by imposing additional or altered obligations on one party to the contract as well as by releasing the other party from his obligations.[62] Moreover, the Court correctly rejected the argument that the state's compelling interest in advancing the welfare of some group—in modern terms the state's use of its police power to advance the public welfare—justified contractual impairments. It is clear from the arguments of both the opponents and proponents of the Clause, that laws designed to advance the welfare of one

shall, the contractual "obligation is not conferred on contracts by positive law, but is intrinsic, and is conferred by the act of the parties." *Id.* at 346.

59. The Justices in the majority believed that the law at the time of contract "whether . . . written or unwritten, . . . is emphatically the law of the contract made within the State, and must govern it throughout, wherever its performance is sought to be enforced." *Id.* at 259.

60. *Id.* at 286 (opinion of Johnson, J.) (emphasis added).

61. Under Chief Justice Marshall's view, the Court could have struck down under the Contract Clause a law limiting the number of hours employees were permitted to work, if the Court determined that employers had a natural right to contract with employees with respect to working hours. In Lochner v. New York, 198 U.S. 45 (1905), the court did strike down state maximum hour legislation as violative of the Due Process Clause.

62. This reading is also supported by the wording of the provision of the Northwest Ordinance on which the Clause was modeled and the wording of the Clause before final stylistic changes were made. *See supra* notes 21-31 and accompanying text.

group at the expense of vested contractual rights were the main target of the Clause.

Nevertheless, the Marshall Court may have erred in its unduly broad construction of the term "contract."[63] Chief Justice Marshall's attempt to subject all executed conveyances to scrutiny under the Contract Clause through the bald assertion that a "grant is a contract executed"[64] is theoretically problematic, and ultimately contrary to the original understanding of the Clause. Marshall claimed that a conveyance contains an implied executory contract that the grantee shall continue to enjoy the subject matter according to the terms of the grant. First, it is apparent that the grantor never made any such promise, and hence, even though the law may constitute a redistribution of wealth between parties to a contract, it cannot truly be said to be a redistribution at odds with the contractual terms.[65] Second, even assuming the parties would have articulated such a promise had they thought of it, the Court is remaking the contract for the parties. Such behavior is contrary to the judicial role.

The Marshall Court also may have erred in expanding the definition of contract to include instruments, like a corporate charter, that reflect types of relationships between a state and its citizens fundamentally different from that represented by a contract.[66] Bona fide contracts for goods and services between a state and its citizens are within the ambit of the Clause.[67] However, the Court's assertion that a contract is created by a grant from the state of any charter, including a corporate charter, confuses the state's prerogative as sovereign to establish the structures that are appropriate for doing business in its territory with its proprietary powers to contract, like any other entity, for goods or services from private individuals. The Contract Clause should apply only to the latter situation, because it is only when the state is acting as a proprietor and receiving consideration that the compacts between the state and a private

63. *See supra* text accompanying notes 41-44 & 52-56.

64. *Fletcher*, 10 U.S. (6 Cranch) at 123.

65. Indeed, as a general matter, once property is conveyed the doctrine of merger by deed may terminate the effect of previous promises not contained in the deed. *See* 6A R. POWELL & P. ROHAN, POWELL ON REAL PROPERTY ¶ 893 (1968).

66. For instance, in *Dartmouth College*, Chief Justice Marshall concluded that the charter for Dartmouth College was within the scope of the Clause. 17 U.S. (4 Wheat.) at 643-44.

67. A distinction between public and private contracts is unwarranted in view of the lack of language limiting the application of the Clause to private contracts or similarly limiting discussion at the Convention. Moreover, given that the overriding purpose of the Clause is to protect rights of parties to a contract from retrospective interference, it does not make sense to exclude from the ambit of the Clause rights that arise from bargains between the state and private individuals. The state legislature, representing the majority, may often have an interest in abrogating the contractual rights of a minority.

individual are comparable to contracts.[68] In its sovereign capacity, the state's ability to reserve the right to amend or revoke a charter or privilege is substantially without limit.[69]

### B. *Stone v. Mississippi* and the State's Police Power

The distinction between the state's governmental and proprietary powers is important to understanding another nineteenth century case which is central to the second period of the Contract Clause's history. In *Stone v. Mississippi*,[70] the Court held that a state could amend a corporate charter to forbid the corporation from selling lottery tickets, despite the fact that the charter had previously granted the corporation the right to conduct lotteries. The Court's decision rested on two separate propositions, either of which, the Court indicated, would have been sufficient to justify its holding. First, since a state legislature could not contract away its power over health and morals, any attempt to do so was void and did not create obligations under the Contract Clause.[71] Second, the right to conduct lotteries was not a property right but a privilege and therefore not within the ambit of the rights protected by the Clause.[72]

Commentators have argued that this case represents the beginning of the Contract Clause's decline.[73] Specifically, by recognizing a police power exception to the Clause, the decision in *Stone* paved the way for the Court's subsequent decision in *Home Building & Loan Association v. Blaisdell*.[74] Once the concept of police power evolved in the twentieth century to include the power to advance the public welfare through redistribution of resources, states could legitimately justify a wide variety of retrospective contractual impairments under the theory advanced in *Stone*.[75]

While this theory accurately describes the way in which *Stone* has been used to justify the contract clause jurisprudence in *Blaisdell*, the

68. A similar point is made in Note, *A Procedural Approach*, *supra* note 4, at 934-37. Of course, it is not always easy to determine when a state is acting in its proprietary, as opposed to its sovereign, capacity. *See generally* Kmiec & Diamond, *New Federalism Is Not Enough: The Privatization of Non-Public Goods*, 7 HARV. J.L. & PUB. POL'Y 321 (1984).

69. *See, e.g.*, Greenwood v. Freight Co., 105 U.S. 13 (1881).

70. 101 U.S. 814 (1879).

71. *Id.* at 819.

72. *Id.* at 821.

73. *See e.g.*, B. SCHWARTZ, CONSTITUTIONAL LAW 189 (1972).

74. 290 U.S. 398 (1934). *See generally supra* text accompanying note 39, and *supra* note 48. In *Blaisdell*, discussed more fully *infra* notes 80-93, the court abandoned the original understanding of the Clause, upholding a type of debtor relief legislation that impaired contractual rights.

75. *See* Sunstein, *Naked Preferences and the Constitution*, 84 COLUM. L. REV. 1689, 1719-20 (1984).

holding in *Stone* does not inevitably lead to *Blaisdell*. Given the original understanding of the Clause, it is certainly possible to believe that *Stone* was correctly decided, while *Blaisdell* and other recent contract clause cases are in error. First, *Stone* may be seen as essentially a correction of the overly expansive reading of what constitutes a public contract. As noted earlier, those cases in which the Marshall Court found a contract between the state and a private party may have been cases in which the state was exercising its sovereign power to order the affairs of its citizens by granting or refusing to grant charters for certain activities.[76] The Court in *Stone* was reaching for such a distinction when it stated that the charter's grant of power to conduct lotteries was not a "property right" but a privilege and thus not protected under the Contract Clause.[77]

Second, the Contract Clause arguably was not framed to restrict unduly the state's police power so long as police power is defined in a way that does not result in the evisceration of the original intent of the Clause. A ban on lotteries, unlike debtor relief, is not designed to redistribute resources in violation of vested contractual rights, but to regulate the morals of the state's citizens. The state's use of its police power to realistically advance some health, safety, or morals interest is unlikely to violate contractual rights in a manner which falls within the prohibition of the Clause.[78] However, once the scope of the police power is expanded to encompass the state's interest in advancing the public welfare (including the improvement of resource distribution), the invocation of police power may often conflict with the original purpose of the Clause. Thus, it is important to define the legitimate scope of the police power in contract clause cases with reference to the original understanding of the Clause rather than to define the Contract Clause by current thinking on the scope of the police power.[79]

### C. The Evisceration of the Contract Clause: *Home Building & Loan Association v. Blaisdell*

In *Home Building & Loan Association v. Blaisdell*,[80] the Court

76. *See, e.g.*, Dartmouth College v. Woodward, 17 15 U.S. (4 Wheat.) 519 (1819).

77. 101 U.S. at 820.

78. For a discussion of the implications of our construction of the Contract Clause for legislation aimed at externalities such as pollution, see *infra* notes 131-133 and accompanying text.

79. For an effort to argue that the scope of police power generally should be construed more narrowly than this under modern doctrine, see R. EPSTEIN, TAKINGS: PRIVATE PROPERTY AND THE POWER OF EMINENT DOMAIN 93 (1985). For a similar limiting construction in the context of land use law, see D. KMIEC, ZONING AND PLANNING DESKBOOK, §§ 2-1 to 2-35 (1986).

80. 290 U.S. 398 (1934).

turned the meaning of the Contract Clause on its head. Influenced by the depression and the growing discontent with the jurisprudence of substantive due process,[81] the Court adopted a very lenient standard of review of debtor relief legislation, despite the fact that such legislation was one of the principal evils which the Clause was designed to prohibit.

The Minnesota statute[82] in *Blaisdell* was not appreciably different from the statutes the Court had invalidated consistently throughout the nineteenth century. The statute provided that a mortgagor who was in default but whose period for redemption of the property had not yet expired could apply to state court for an extension of the redemption period. The Court required the petitioner to pay a reasonable rent for the extension period and part of these payments could be applied to the interest on the debts that the applicant owed. Pursuant to the statute, the state court extended the redemption period for three years, from May 2, 1932 to May 1, 1935, and ordered Mr. Blaisdell to pay forty dollars a month in rent.

Writing for a narrow majority of five Justices, Chief Justice Hughes stated explicitly that the Court was not bound by the original understanding of the Clause. Rather, Hughes posited that the Court must consider the case " 'in the light of our whole experience and not merely in that of what was said a hundred years ago,' "[83] and that because of a "growing recognition of public needs . . . the reservation of the reasonable exercise of the protective power of the State is read into all contracts . . . ."[84]

81. For a discussion of popular criticism of the Supreme Court in the early 1930's, see M. KAMMEN, A MACHINE THAT WOULD GO OF ITSELF: THE CONSTITUTION IN AMERICAN CULTURE 259 (1986).

82. 1933 Minn. Laws ch. 339.

83. *Blaisdell*, 290 U.S. at 443 (quoting Missouri v. Holland, 252 U.S. 416, 433 (1920)).

84. *Id.* at 443-44. The opinion in *Blaisdell* purported to find important support for its holding in Charles River Bridge v. Warren Bridge, 36 U.S. (11 Pet.) 420 (1837) and West River Bridge Co. v. Dix, 47 U.S. (6 How.) 507 (1848), as well as Stone v. Mississippi, 101 U.S. 814 (1879). None of those authorities were particularly apposite. The principal holding in *Charles River Bridge* was the rule that public contracts should be narrowly construed in favor of the state. This holding can be seen as a reaction to the Marshall Court's overly expansive view of what is a contract and, in any event, was not meant to govern review of private contracts. *West River Bridge Co.* held under the reserved powers doctrine that a state could not alienate through contract its powers of eminent domain. Therefore, the state has the right to appropriate contractual rights, like other property rights, so long as just compensation is paid. The state eminent domain power, unlike the power exercised in *Blaisdell*, is wholly consistent with the purpose of the Contract Clause. No redistribution occurs because compensation is paid for the voiding of vested contractual rights. We have already noted that in *Stone v. Mississippi* the legislation, unlike that at issue in *Blaisdell*, did not redistribute resources from one party to another. *See supra* text accompanying notes 70-79.

The Court upheld the statute in *Blaisdell* after finding that it met five criteria. First, the Court noted that the statute was emergency legislation passed in response to an economic crisis.[85] Second, the Court stated that the object of the legislation was the protection of "a basic interest of society," not the "advantage of particular individuals."[86] The third and fourth criteria blended together to assert that the relief be granted according to reasonable conditions because (1) the integrity of the mortgage was not impaired, and (2) the mortgagor was required to pay the mortgagee a reasonable rent for the period in which the redemption was extended.[87] Finally, the Court noted that the legislation was temporary in operation.[88]

Justice Sutherland's dissent argued that the majority ignored the original understanding of the Clause and embraced the arguments of those who opposed the Clause at the Convention and in the ratification debates. As noted above, one opponent, Luther Martin of Maryland, had argued for the necessity of state power to address the condition of the debtor, particularly in periods of economic crisis.[89] However, the Clause was framed immediately following a time in which debtor relief laws were frequently passed in response to perceived economic emergencies. Thus, the Clause was included in the Constitution to protect vested contract rights precisely during those times of crisis in which the *Blaisdell* Court would permit impairment. As Justice Sutherland stated, "With due regard for . . . logical thinking, it legitimately cannot be urged that conditions which produced the rule may now be invoked to destroy it."[90]

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85. 290 U.S. at 444.

86. *Id.* at 445.

87. *Id.*

88. *Id.* at 447.

89. *See supra* note 34.

90. *Blaisdell*, 290 U.S. at 472 (Sutherland, J., dissenting). Justice Sutherland also sharply attacked the majority's argument that the constitutional text should be reinterpreted in light of experience. In a classic statement of a jurisprudence of original intent, he argued:

> A provision of the Constitution, it is hardly necessary to say, does not admit of two distinctly opposite interpretations. It does not mean one thing at one time and an entirely different thing at another time. If the contract impairment clause, when framed and adopted, meant that the terms of a contract for the payment of money could not be altered *in invitum* by a state statute enacted for the relief of hardly pressed debtors to the end and with the effect of postponing payment or enforcement during and because of an economic or financial emergency, it is but to state the obvious to say that it means the same now. This view, at once so rational in its application to the written word, and so necessary to the stability of constitutional principles, though from time to time challenged, has never, unless recently, been put within the realm of doubt by the decisions of this court.

*Id.* at 448-49.

The other criteria relied on by the majority are no more satisfactory than the majority's invocation of an emergency. The argument that this legislation advanced a basic public interest rather than a private interest is unpersuasive. As we have seen, the debtor's attorney made the same argument in *Sturges v. Crowninshield*,[91] but it was not accepted by the Court.[92]

The Court's emphasis on the reasonableness of the conditions attached to the legislation was also misplaced. The Court read the Clause as if it stated: "No state shall pass any law unreasonably impairing the obligation of contracts." The Framers, however, knew how to phrase prohibitions in terms of reasonableness, as shown by the Fourth Amendment's prohibition against "unreasonable searches and seizures." The Contract Clause is phrased in absolute terms and is grouped with other absolute prohibitions such as the Bill of Attainder and Ex Post Facto Clauses designed to protect the rule of law. Therefore, a contract clause jurisprudence that adheres to the original understanding must either strike down all retrospective impairments or, like first amendment jurisprudence, create an exceedingly stringent standard of review that only the most compelling demonstrations of necessity will satisfy.

More than anything else, *Blaisdell* shows the power of the *Zeitgeist* to determine constitutional decisions even when those decisions are demonstrably at odds with any original understanding of the Constitution. The legitimate attack on substantive due process erroneously led to a new unified theory of the Constititution—that it never, or almost never, constrains economic legislation.[93] The theory proceeded on the misapprehension that the Contract Clause, like substantive due process, was a threat to representative government. To the contrary, the Contract Clause, like the Bill of Attainder and Ex Post Facto Clauses, is designed to protect minority factions from majority oppression by enforcing the rule of law, and is thus consistent with the theory of representative government that the Framers held. Therefore, the vigor with which the Clause is enforced should not have diminished with the demise of substantive due process.

### D. Current Contract Clause Jurisprudence

The Court under former Chief Justice Burger revived the Contract Clause to a limited extent by adopting a more stringent standard of re-

91. 17 U.S. (4 Wheat.) 122 (1819).

92. *See supra* note 50.

93. For a discussion of the reasons that substantive economic due process was attacked, see *infra* notes 124-125 and accompanying text.

view for certain contractual impairments. As a result, the Court has, invalidated statutes under the Clause for the first time since the late 1940's.[94] The revival of the Clause, however, falls far short of restoring it to the power it should enjoy, given the original intention of the Framers. Moreover, the present Court's jurisprudence is at odds with the Framers' interest in providing certainty to those who enter into contracts, because in evaluating the constitutionality of an impairment the Court has adopted widely differing standards of review and balanced the extent of the impairment against the policy that the state seeks to advance. Based on an ad hoc policy calculus, the Court's decisions are largely unpredictable.

The Court's decision in *United States Trust v. New Jersey*[95] marks the beginning of the most recent period of contract clause jurisprudence. In that case, the states of New York and New Jersey had passed a bill abrogating a provision of a covenant in a bond agreement. The provision had limited the ability of the Port Authority, an interstate compact agency, to subsidize passenger transportation from revenues which had been pledged as securities to Port Authority bondholders.[96] The purpose of the abrogation was to permit the Port Authority to subsidize commuter rail services to a greater extent.[97]

Justice Blackmun's analysis began by suggesting that ordinarily "[s]tates must possess broad power to adopt general regulatory measures without being concerned that private contracts will be impaired, or even destroyed, as a result."[98] He described the proper standard of review of legislation challenged under the Contract Clause as one which would uphold as constitutional impairments that are "reasonable and necessary to serve an important public purpose."[99] Moreover, Justice Blackmun noted that courts should defer to legislative judgments as to the reasonableness of particular measures, as they defer in their due process review of economic legislation.[100] Thus, Justice Blackmun implied that in the

94. *See* Allied Structural Steel v. Spannaus, 438 U.S. 234 (1978); United States Trust v. New Jersey, 431 U.S. 1 (1977).

95. 431 U.S. 1 (1977).

96. This is clearly an example of a public contract in which the state is acting in its proprietary capacity, because the state is attempting to borrow money from private individuals. As an inducement to the bondholders, the state has entered into a covenant to secure the revenues from which interest on the bond is paid.

97. 431 U.S. at 14.

98. *Id.* at 22. Justice Blackmun denominates this power as "the reserved power doctrine." The doctrine states that a "reasonable exercise of the protective power of the State is read into all contracts. . . ." Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 444 (1937).

99. 431 U.S. at 25.

100. *Id.* at 22-23.

usual case the standard of review will be very lenient. However, Justice Blackmun then distinguished the usual case in which the contract impaired is between private parties, from the case in which the contract impaired is one to which the state is a party. Although Justice Blackmun believed that both private and public contracts should be reviewed under the same formulation of "reasonable and necessary," he argued that the standard should be applied with less deference in reviewing public contracts because "the State's self-interest is at stake."[101] Justice Blackmun then adopted a least restrictive alternative analysis of New Jersey's abrogation of the covenant.[102] Because he concluded that a less drastic modification would have permitted the Port Authority to increase public transportation without entirely abrogating the covenant, he held the state legislation invalid.[103]

Each of the steps in Justice Blackmun's lengthy effort to establish and apply a standard of review is open to criticism. First, in constructing a test that seeks to determine which impairments are constitutional, the Court ignores the plain language of the Contract Clause. According to that language, once legislation is found to impair a contract it violates the Clause. The structure of Justice Blackmun's test evinces a balancing approach that, at its foundation, is contrary to the absolute language of the Clause.

Second, Justice Blackmun's phrasing of the standard of review as a determination of whether the legislation impairing the contract is "reasonable and necessary" to effectuate an important public purpose is both curious and confusing. A reasonableness test is a fairly relaxed or minimal standard of constitutional review while formulations employing necessity have been viewed as calling forth a more exacting standard.[104] Justice Blackmun confuses the issue further when he suggests that in the ordinary course the Court will defer to state determinations of what is "reasonable and necessary." Such deference seems to collapse the stan-

101. *Id.* at 26. To support this distinction, Justice Blackmun argued that the scope of the police power reserved to the state in contract clause cases has been determined under two distinct analyses depending upon whether the contract is private or public. According to Justice Blackmun, in cases involving private contracts the relevant inquiry is what powers are reserved by the state as a matter of law in construing any contract. *See, e.g.*, Manigault v. Springs, 199 U.S. 473, 480 (1905). In public contracts, the initial inquiry is into whether the state may bargain away the police power at issue or whether that power is "inalienable." *See* Stone v. Mississippi, 101 U.S. 814, 817 (1879). While the doctrines of "reserved powers" and "inalienability" may indeed be nominally distinct, there has never been any suggestion that the powers reserved are different from the powers inalienable. Certainly no case under either doctrine previously suggested that one standard of review is to be distinguished from another.

102. 431 U.S. at 28-32.

103. *Id.* at 30-32.

104. *See id.* at 54 & n.17 (Brennan, J., dissenting).

dard of review, whatever the formulation, into the rational basis test for economic legislation under the Due Process Clause and thus deprives the Contract Clause of any independent force. Justice Blackmun's mixing of standards demonstrates a schizophrenia that characterized the Burger Court's approach to review under the Contract Clause: the Court wanted to apply a stringent standard in order to respect the Constitution's expressed solicitude toward contractual rights, and to simultaneously keep the standard relaxed so that it would be consistent with the relaxed standard that has come to characterize the Court's review of economic legislation. These mutually inconsistent goals, fostered by an assumed, but mistaken, identity between the concerns of substantive due process and the Contract Clause, have created an incoherent jurisprudence.

Justice Blackmun's attempt to raise the standard of review for legislation which impairs public contracts above that for legislation which impairs private contracts is also in error. First, a more stringent standard of review for public contracts is not supported by the text or history of the Contract Clause. If anything, the Court's earlier jurisprudence has been more, not less, deferential to public contracts insofar as the contracts were more likely to implicate the police power or reserved authority. Second, while the argument that the legislature's self-interest in public contracts should lead to a stricter review has a certain, albeit delusive, plausibility, it is fundamentally incorrect because the self-interest of a state legislature passing economic or social legislation is, at bottom, no different from the public interest. The state invokes the same justifications for modifying public contracts and private contracts—namely, that the public welfare will be advanced by the alteration—and the alteration should be reviewed under the same standard.[105]

The Court's opinion in *United States Trust* is almost Ptolemaic in nature: that is, it represents a very complex, and ultimately incorrect, theory to explain a result that on a true understanding of the Clause is apparent. A state's abrogation of a bond covenant into which its port authority expressly has entered to induce people to buy bonds voids a contractual provision. The state's justification of the abrogation is consciously redistributive; if the bondholders' contractual rights are sacrificed the commuting public will be aided because the Port Authority can subsidize more commuter railroads. Because the abrogation of the bondholders' covenant is retrospective and consciously redistributive, it is contrary to the Contract Clause.

105. *See* Comment, *Repeal of Municipal Bond Covenants*, 91 HARV. L. REV. 83, 89-90 (1977).

The Court's other recent contract clause decisions do not construct such an elaborate standard of review, but more explicitly engage in balancing the state's interest in abrogating a term of the contract and the contract holder's interest in maintaining its terms. In *Allied Structural Steel v. Spannaus*,[106] the Court faced the issue of whether Minnesota could order corporations with pension plans to pay pension benefits to employees whose benefits had not yet vested under the terms of the contract between the corporation and its employees. Writing for a five member majority, Justice Stewart undertook a balancing approach to determine whether this legislation could withstand scrutiny under the Contract Clause. First, Justice Stewart assessed the severity of the contract impairment, because, according to Justice Stewart, "[t]he severity of the impairment measures the height of the hurdle the state legislation must clear."[107] Because the vesting provisions were a basic provision of the pension plan agreed to by the corporation and its employees, and because the company reasonably relied on these provisions in calculating its annual contributions to the pension fund, the Court found a severe impairment.[108] As for the state's interest in enacting the legislation, the Court noted that whereas the mortgage moratorium legislation at issue in *Blaisdell* had protected a broad societal interest, the pension vesting legislation protected the interests of only a "narrow class" of employees.[109] The legislation applied only to private employers who had at least 100 employees and who had established voluntary pension plans. Moreover, the legislation was not enacted to deal with an economic emergency like that which prompted the mortgage moratorium legislation in the 1930's. Therefore, after balancing the state's interest in passing the legislation and the company's interest in maintaining the terms of its contract, the Court struck down the legislation.[110]

*Allied Steel* reached the correct result through unprincipled reasoning. Justice Stewart's test led to a different result from *Blaisdell* only because the majority subjectively had assigned different weights to the factors to be balanced. To be sure, the vesting provisions were central to the contract between the corporation and its employees, but no more so than foreclosure and redemption provisions were central to the mortgage contract. While it is true that no general economic emergency existed in

106. 438 U.S. 234 (1978).

107. *Id.* at 245.

108. *Id.* at 246.

109. *Id.* at 249.

110. Justice Stewart never explicitly stated that he was employing a balancing test but the structure of the opinion—first evaluating the contract holders' interest and then the state's interest—demonstrates that this is a fair characterization of his mode of analysis.

the mid-1970's, many experts believed that there was a crisis in pension plan administration because employees were being denied the possibility of a secure retirement by pension plans that raised false expectations of benefits.[111] Finally, it is unclear why the state's interest in giving employees secure pension plans is less compelling than its interest in saving their homes. It is true that there may be more people who have mortgages than who have pension plans of the kind at issue in *Spannaus*. Yet an analysis that upholds legislation in proportion to the number of people who will benefit by the impairment seems wholly contrary to the original understanding of the Clause if we remember that debtor relief legislation—a primary target of the Clause—affected a very large group of people, namely debtors. It also is contrary to the Clause's underlying purpose: the protection of an isolated minority faction (those who stand to benefit from the contract to be altered or abrogated) from majority oppression. When the abrogation or modification of a contract will benefit many people rather than just a few, majority oppression is more likely and therefore the strictures of the Clause must be vigorously enforced.[112]

The lack of a principled approach to the Contract Clause was highlighted when the Court relaxed its standard of review to uphold an impairment of contract in *Exxon Corp. v. Eagerton*.[113] In *Exxon*, the Supreme Court refused to invalidate Alabama legislation that prevented a producer of oil and natural gas from passing on increases in a severance tax to buyers in bulk of natural gas, according to explicit contrac-

111. The perception of this crisis was so widespread that it led to the passage of the Employee Retirement Income Security Act of 1974, Pub. L. No. 93-406, 88 Stat. 829. *See* H. Rep. 127, 1st Sess. 1, 7-8 (1973) (provisions of ERISA are "addressed to the issue of whether working men and women shall receive private pension plan benefits which they have been led to believe would have been theirs upon retirement from working lives").

112. In Note, *Rediscovering the Contract Clause*, *supra* note 13, at 1426-28, the author argues that the approach in *Allied Steel* is consistent with an understanding of the Contract Clause as an attempt to protect the rule of law or what the writer terms "institutional regularity." The argument seems to depend on the proposition that legislation impairing contracts offends the rule of law in proportion as it favors or disfavors an identifiable class. This proposition, in turn, is derived from the ideal of generality in the rule of law.

This theory of the Contract Clause is open to question as a matter of original understanding and would be impossible to apply in any principled manner. First, while generality is an ideal of the rule of law, the legislation's generality does not ameliorate its retrospectivity. The Bill of Attainder Clause, for instance, was included in the Constitution to protect against laws of improper specificity, but the history of the Contract Clause strongly suggests that the Clause was intended to protect contracts against retrospective legislation regardless of the legislation's generality. Moreover, it is difficult to understand how the decisions under the Contract Clause can turn on the issue whether those helped or hurt by an impairment form an identifiable class. Contractual impairments by their very nature affect identifiable classes— those who are parties to the contracts impaired.

113. 462 U.S. 176 (1983).

tual terms permitting the seller to pass on the tax. The Court rested its holding on two propositions. First, it distinguished its holding in *Allied Steel*, finding that the Alabama legislation in *Exxon* was motivated by a broad local interest—that of preventing consumers from paying excessive prices.[114] Second, the Court seemed to suggest that this legislation did not violate core expectations of the parties to the contract because the states have always enjoyed plenary power to set rates, particularly in regulated industries such as natural gas. Therefore, the Court concluded that if a party is not immune from regulation of rates, it is not immune from state legislation regulating the incidence of a tax on a preexisting contract.[115]

Once again, the Court manipulated its standard of review and weighted its balances in order to reach the desired result. First, the standard was formulated far differently from the one articulated in *United States Trust*, in which the Court required impairments to be both reasonable and necessary. Second, the Court's distinction of *Allied Steel* on the ground that the Alabama legislation in *Exxon* served a broader interest than the pension plan legislation is not compelling. It is wholly unclear on what basis a court is to decide whether a state's interest in protecting a worker's retirement security is less important than protecting consumers from higher prices. Of course, it is true that the interest is broader in that there are more oil consumers than those covered by pension plans, but, as already suggested, gauging the number of those who are aided or hurt by the impairment is an unprincipled guide to whether the impairment is constitutional.

Finally, the Court's reliance on a state's ability to set prices in a heavily regulated and monopolistic industry like utilities does not serve as a compelling precedent for the state to regulate the incidence of severance tax among those in the chain of distribution of a particular commodity. In other words, the government has made clear that because utility rates will be set by regulation, utility companies do not possess a contractual right to receive a particular price. Both on account of the monopolistic structure of utility companies and because of the tradition of regulation, it may be possible to argue that utility companies are on notice that prices to consumers may be regulated even in contravention of a contract. The fact that the state government sets utility rates, however, does not imply that those who have contracted to determine the incidence of a tax are on notice that they do not possess contractual

114. *Id.* at 191-92.
115. *Id.* at 194.

rights under positive law.[116]

A more principled approach to the contractual impairments faced by the Court in *Allied Steel* and *Exxon* would have eschewed manipulation of standards and weighted scales. In *Allied Steel*, the Court should have observed that the corporation and its employees had obviously agreed on a pension plan between themselves. They had bargained for contractual provisions which, *inter alia*, set out periods in which the pensions were to vest. By requiring the company to pay pensions to employees who were not qualified under this plan, the state was impairing a specific provision of the bargain. Moreover, the legislation could not be justified by reference to a concept of police power consistent with the original understanding of the Contract Clause, because the legislation was frankly redistributive. Therefore, the retrospective effect of the pension legislation in *Allied Steel* was inconsistent with the Contract Clause. Similarly, the legislation in *Exxon* altered a specific provision of the contract between buyer and seller of natural gas and oil. The legislation cannot be justified by a concept of police power that is consistent with the Contract Clause[117] nor do other justifications exist, as the state had never explicitly or by tradition reserved to itself the power to revise contracts by determining where the incidence of a tax falls. Therefore, the abrogation of the pass-through provisions should have been invalidated under the Contract Clause.

In *Keystone Bituminious Coal Association v. DeBenedictus,*[118] a case decided just this Term, the Court has signalled that it will continue to adhere to its unprincipled contract clause jurisprudence. In that case, mine owners who had contracted with surface owners to waive liability for surface damage challenged under the contract clause legislation which prohibited the licensing of mine owners unless they repaired all subsidence damage which their mining had caused to surface lands.[119] Justice Stevens, writing for the Court, summarily rejected the challenge, first observing without explanation that, unlike all the other prohibitions imposed on the states by article I, section 10 of the Constitution, "it is well-settled that the prohibition against impairing the obligation of contracts is not to be read literally."[120] Accordingly, the Court held that

116. Similar criticism may be levied against Energy Reserves Group, Inc. v. Kansas Power & Light Co., 459 U.S. 400 (1983), in which the Court refused to strike down legislation which abrogated price redetermination clauses in a contract between a utility and supplier of natural gas.

117. *See supra* notes 78-79 and accompanying text.

118. 107 S. Ct. 1232 (1987).

119. The mine owners also brought a challenge under the Takings Clause. *Id.* at 1236.

120. *Id.* at 1251.

although the statute was a contractual impairment, it was justified by the "strong public interest in preventing [subsidence damage caused by mining], the environmental effect of which transcend[s] any private agreement between contracting parties."[121] The Court also continued to employ a confused standard to evaluate the state's asserted justification of the impairment, first arguing that a court must itself scrutinize whether the legislature's action was appropriate in light of its purpose, and then stating, one sentence later, that the courts should defer to the legislature's judgment as to the necessity of its action.[122]

*Keystone* demonstrates that the Court believes it can now dispose of a serious contract clause claim in a few conclusory paragraphs without even discussing its own inconsistent standards of review.[123] Thus, the revival of the Contract Clause, which began with *United States Trust* and *Allied Steel*, appears to have ended, in large measure because these cases failed to rediscover the original understanding of the Clause. A return to the original understanding, we believe, would provide a coherent jurisprudence for contract clause cases.

## IV. Possible Criticism of the Original Understanding

In brief, an accurate construction of the Contract Clause would invalidate retrospective, not prospective, laws which are redistributive in violation of vested contractual rights. A revival of the original understanding of the Contract Clause may be challenged as a return to substantive due process analysis. As alluded to earlier and more fully discussed below, we believe this challenge to be baseless. The proposed construction may also be criticized both for its breadth and its narrowness. Those criticizing its breadth will likely argue that the interpretation we suggest renders the operation of the modern welfare and regulatory state difficult, if not impossible. On the other hand, those criticizing its narrowness may contend that our refusal to apply the Clause to prospective legislation insufficiently protects economic liberties. We will briefly address each of these possible criticisms.

### A. Substantive Due Process

To equate the original understanding of the Contract Clause to substantive due process is to misunderstand both concepts. To see why this is so, it is useful to summarize why substantive due process, particularly

121. *Id.* at 1252.

122. *Id.* at 1253.

123. For a discussion of the proper resolution of the facts presented by *Keystone*, see *infra* text accompanying notes 134-135.

as it relates to the judicial invalidation of social and economic legislation, has been fairly criticized. There are three main lines of criticism which, although interrelated, may be separately stated. First, substantive due process has little or no historical basis. There is little evidence that the ratifiers of the Fourteenth Amendment intended to give courts the right to invalidate social and economic legislation because of perceived interference with some set of economic theories.[124] Second, because it rests on no demonstrable textual or historical principle of the Constitution, substantive due process results in an unprincipled jurisprudence in which the Court upholds or overturns economic and social legislation on the basis of an unpredictable policy calculus of the reasonableness of the legislation's interference with economic liberty.[125] Third, substantive due process is undemocratic because it permits unelected judges to overturn the decisions of the people's representatives on essential matters of social and economic policy.

The construction of the Contract Clause posited here suffers from none of these defects. First, it has substantial support in the history of the Clause. Second, the construction asserted, unlike that currently employed by the Court, eschews ad hoc balancing by invalidating all legislation that retrospectively alters the terms of an existing bargain between contracting parties in an attempt to redistribute resources. Third, this interpretation is consistent with the concept of democracy that the Framers actually possessed—a democracy constrained by the rule of law.[126]

### B. Inconsistency with the Modern Regulatory and Welfare State

Even though the Framers' theory of the Clause may be distinguished from substantive due process, some may argue that it gives too much protection to economic interests to be consistent with the modern regulatory and welfare state. Without passing judgment on the validity of the premise underlying this position—namely, that constitutional provisions should be accommodated to the form of government currently perceived as necessary or desirable notwithstanding the ascertainable meaning of these provisions—we believe that the original understanding

124. For a discussion of the original understanding of the Fourteenth Amendment, see R. BERGER, GOVERNMENT BY JUDICIARY 193-220 (1977). The classic statement of the Fourteenth Amendment's agnosticism toward competing economic theories is Justice Holmes' dictum, "[t]he 14th Amendment does not enact Mr. Herbert Spencer's Social Statistics." Lochner v. New York, 198 U.S. 45, 75 (1905) (Holmes, J., dissenting).

125. For a discussion of the reasons substantive due process leads to unprincipled judicial decisionmaking, see Bork, *Neutral Principles and Some First Amendment Problems*, 47 IND. L.J. 6-15 (1971).

126. *See supra* notes 10-13 and accompanying text.

of the Contract Clause does not render the modern regulatory and welfare state impossible.

To be sure, under the interpretation of the Contract Clause discussed here, state and local legislatures would be disabled from passing laws that modified contracts between parties in the interest of helping one party to the contract at the expense of the other.[127] Thus, some modern legislation presently upheld by federal courts would be invalid under the original interpretation of the Clause. For instance, a federal court recently upheld the application to existing dealership contracts of a state law requiring that a dealer be given a six month opportunity to cure performance before cancellation for poor performance.[128] Such an application clearly violates the Contract Clause because under the law at the time of acceptance of the contract, manufacturers could terminate their contracts with dealers at will unless other terms were specified in the contract. Similarly, a local law retrospectively giving a tenant rights not contained in his or her lease, such as the right to remain a tenant after the building is converted into a condominium, would be unconstitutional.[129] This interpretation of the Clause would also generally prevent the retroactive application of rent controls.

States and localities would not be permanently prevented from applying such legislation, however, because under the interpretation posited, states and localities remain at liberty to apply prospectively all the laws in the examples cited above. This interpretation does not forbid changes in any social institution, whether pertaining to marketing distribution, rental housing, or other subjects, if such changes are perceived to be required by social needs. If a legislature believes that such changes are needed immediately, nothing in the interpretation suggested prevents the legislature from buying out contractual obligations under its eminent domain power so that the cost of voiding the obligation is borne by the community as a whole rather than by those who stand to benefit from the obligations voided.[130] Moreover, our interpretation of the Clause does

127. The legislation need not display a specific intent to redistribute before it should be deemed to violate the Contract Clause. If the necessary consequence of the legislation is to redistribute resources between parties to a contract, an intent to redistribute may be inferred and the legislation should be subject to strict scrutiny under the Contract Clause.

128. *See* N.A. Burkitt, Inc. v. J.I. Case Co., 597 F. Supp. 1086 (D. Me. 1984).

129. *See* Troy Ltd. v. Renna, 727 F.2d 287 (3d Cir. 1984) (upholding against a contract clause challenge a tenancy act which retrospectively conferred on citizens over sixty years of age special rights with respect to evictions upon condominium conversions).

130. In addition, not all retrospective laws are prohibited; only those that impair contractual rights actually violate the Clause. For example, a recent California law requires that the owner of fine art pay five percent of any resale amount to the artist from whom he bought the work. *See* Morseburg v. Balyon, 621 F.2d 972 (9th Cir.), *cert. denied*, 449 U.S. 983 (1980). As

not forbid regulations aimed at economic externalities even if the legislation has the incidental effect of rendering contractual performance more difficult or even impossible.[131] For instance, consider legislation that requires the use of pollution controls on widget factories. Because of the introduction of pollution controls, the widget manufacturer may lose money on his or her outstanding contracts to widget buyers. Nevertheless, this legislation violates neither the letter nor spirit of the Contract Clause. It is not the *necessary* consequence of the legislation that the widget manufacturer, rather than the widget buyer, bears the added cost of pollution controls; the manufacturer and buyer could have contractually agreed to have the manufacturer pass the costs on to the buyer. Accordingly, the manufacturer suffers a loss not because of the impairment of the contractual obligation, but by operation of the contract.[132] Nor does legislation exclusively aimed at externalities generally have the effect of conferring a benefit on one party to the contract at the expense of another: the widget buyer, unlike the failing dealer or tenant in our previous examples, does not directly gain from the imposition of pollution controls. For this reason, legislation aimed at externalities is unlikely to be of the kind that Madison believed the Contract Clause was designed to prevent— that is, legislation produced by a faction interested in interfering with contractual obligations for its own benefit.[133]

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we have earlier rejected Chief Justice Marshall's attempt in *Fletcher v. Peck* to convert property rights into contract rights by finding implied promises in contracts that have already terminated, *see supra* notes 63-65 and accompanying text, the California law would not appear to be a contractual impairment. After the "objet d'art" has changed hands, the law is better understood as an impairment of a property, rather than a contract, right. If state regulation like that suggested by the California law is to be constrained, the proper judicial focus would be a takings analysis, either under the state constitution or under those federal taking principles which have been incorporated by the Court as part of the Fourteenth Amendment Due Process Clause.

131. An externality is the social cost of an activity that the market's pricing system fails to include in the price of the activity, because the transaction costs of bargaining over the ownership of the rights affected by the activity exceed the social costs the activity imposes. *See generally* Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960). For instance, the transaction costs of reaching an agreement between a polluter and those who may be harmed by the polluter's activity would be very high. Retrospective legislation addressed to the problem of externalities will not necessarily violate the Contract Clause because by hypothesis externalities are caused by an inability of parties to allocate costs through contractual arrangements.

132. This example also makes clear the reasons that legislation interfering with the allocation of the costs of regulation, such as the legislation at issue in *Exxon Corp. v. Eagerton*, 462 U.S. 176 (1983), violates the Contract Clause. Because the Contract Clause was designed to permit people to plan for the future through their ability to create vested rights, legislation that invalidates the allocation of costs of unexpected legislative action makes a mockery of the contract clause promise of a safe harbor against the unpredictable will of the legislature.

133. Of course, regulation ostensibly designed to internalize externalities can be employed through manipulation or capture of the regulatory or legislative process by one competing

Of course, like all useful interpretations of constitutional clauses, this interpretation of the Contract Clause will not avoid hard cases. For instance, consider state legislation requiring that when coal mine operators reduce the value of surface land above their mines they must restore the land to the extent technologically feasible. The state claims that this legislation is needed to protect the state's interest in the environment.[134] Previously, mine operators bought mineral rights from a large number of landowners and, as part of these transactions, the landowners also waived any right to damages that the mining would cause to their surface. Does this legislation, as applied to land with respect to which such contractual waivers exist, violate the Contract Clause? On the one hand, the natural consequence of the legislation, unlike that in the pollution-widget example above, seems to be to redistribute resources from the mine operators to the landowners in contravention of vested rights. On the other hand, however, the state's purported justification is that the legislation is designed to protect the ostensible rights of third parties—the people of the state—to enjoy the environment.

The difficulty stems from the fact that there is a direct correlation between the public good that the state seeks to protect—the environment—and the private right that the landowner has bargained away—the right to avoid damage to the land's surface. To protect the public good is to abrogate the landowner's contractual waiver. Despite the social justification for the legislation, the landowner is the beneficiary of the wealth redistribution. One traditional mode of analysis that the judiciary employs to ensure that legislation passed for an ostensibly legitimate purpose does not encroach on constitutional rights is the least restrictive alternative analysis.[135] This approach may be appropriate here. By re-

party to disadvantage another. For example, one way natural gas companies may augment business is to portray a competing fuel like high-sulphur coal as environmentally harmful, thereby triggering the stringent regulation of coal usage. While it may be desirable to create systemic barriers to such rent-seeking behavior, *see infra* note 138, courts are ill-suited to undertake such policy-laden action, unfocused as it would be in most cases on the impairment of specific contractual obligations.

134. *See* Keystone Bituminous Coal Ass'n v. Duncan, 771 F.2d 707 (3d Cir. 1985) (rejecting a contract clause challenge on similar facts), *aff'd sub nom.* Keystone Bituminous Coal Ass'n. v. DeBenedictus, 107 S. Ct. 1232 (1987). The *Keystone* decision is discussed *supra* at text accompanying notes 118-123

135. Least restrictive alternative analysis has been applied in a number of areas to require that government, when it has available a variety of equally effective means to a given end, must choose the alternative that least interferes with constitutional rights. *See* Note, *Less Drastic Means and the First Amendment*, 78 YALE L.J. 464 (1969). Examples of cases in which the doctrine has been applied include Aptheker v. Secretary of State, 378 U.S. 500, 507-08 (1964) (right to travel); Shelton v. Tucker, 364 U.S. 479 (1960) (First Amendment); Dean Milk Co. v. City of Madison, 340 U.S. 349, 354 (1951) (Commerce Clause).

quiring the landowner rather than the mine operator to restore the land in cases where the landowner has waived his or her right to damages, the state could accomplish its goal of preserving the environment without impairing vested contractual rights. Accordingly, in cases in which legislation impairs contractual obligations in the interest of eliminating economic externalities, courts must consider carefully whether any alternative exists that would permit the legislature to meet its regulatory objective without impairing obligations vested by contract.

The Contract Clause, correctly construed, thus will not prevent a state ultimately from regulating activities as it wishes, but it may prevent a state from imposing the costs of regulation without regard for vested contractual rights. It is not a barrier to social change; it simply constrains that change to be consistent with the rule of law.

### C. Prospective Application of the Clause—A Response to Professor Epstein

Professor Richard Epstein has argued in a recent article that, notwithstanding the decision in *Ogden*, the Clause should be read as applying prospectively—*i.e.*, to interferences with future contractual opportunities as well as to impairments of existing obligations.[136] Professor Epstein can scarcely rely upon the text and the history of the Clause at the Convention and in the ratification process for this proposition.[137] His stronger and more elaborate argument derives from his view that the overriding purpose of the Contract Clause, consonant with the overriding purpose of the Constitution, is to prevent "rent-seeking behavior," the product of which is legislation that redistributes wealth from one group to another.[138] Professor Epstein argues that legislators are as likely to redistribute wealth by the use of prospective interferences with contractual opportunities as by retrospective interferences with rights that have become vested under positive law. Moreover, the consequences of prospective interference with contractual opportunities may be as damaging as retrospective interferences, because expectations that have not yet crystallized into vested rights may nevertheless be of enormous

136. *See* Epstein, *Toward a Revitalization of the Contract Clause*, 51 U. CHI. L. REV. 703, 723-730 (1984).

137. We have already explained how the history of the Clause at the convention and in the ratification process supports our view of its interpretation. See *supra* notes 9-29 and accompanying text.

138. Professor Epstein argues that the danger of oppression of minority rights that Madison outlined in *The Federalist* is best characterized in modern terms as the danger of rent-seeking behavior. *See* Epstein, *supra* note 136, at 713 (defining "rent-seeking" behavior as the tendency of each interest group to use legislative power to expropriate the wealth of its rivals).

importance to the individual. Therefore, Professor Epstein believes that the rationale of the Clause applies equally to retrospective and prospective legislation.[139]

Clearly, prospective legislation can have a redistributive effect. Nonetheless, there are fewer natural barriers to rent-seeking legislation that is retrospective in character than to that which is prospective. When contractual rights and obligations have been fixed, the winners and losers from the enactment of a bill affecting such rights are apparent and fall in a well-defined and narrow class. For example, debtors will benefit from debtor-relief legislation: the loss falls entirely on the creditors. As the legislation becomes prospective, however, the affected class is less narrowly defined. To use two examples that Professor Epstein believes should be subject to the strictures of the Contract Clause, legislation that forbids opticians from fitting eyeglasses without an optometrist's prescription not only depresses the income of opticians but raises the prices of glasses for consumers; legislation raising the minimum wage decreases not only the value of property leased at long-term by labor intensive businesses but disadvantages consumers to whom the leaseholder will likely pass on any extra costs.[140]

Unlike those affected by retrospective impairments, these two brief examples reveal that those adversely affected by prospective legislation should more readily find allies against the oppression of a faction seeking the passage of self-serving legislation designed merely to redistribute wealth to itself. Given the Framers' particular concern to prevent situations in which minority factions would be isolated and therefore easily oppressed, it makes sense to erect special barriers against retrospective

139. Professor Epstein suggests that a retrospective reading of the Contract Clause would lead to its ultimate vitiation, because states could simply pass so-called "reservation" statutes, which would reserve to the legislature the right to make any changes it wished in any contracts executed after the passage of the statute. We believe that "reservation" statutes of such breadth would be unconstitutional, because they would constitute a blatant attempt to statutorily repeal the Contract Clause from our constitutional scheme. The statutes would be a declaration that the legislature could exercise arbitrary will despite the fact that the Clause was introduced to prevent such arbitrariness. *See supra* text accompanying notes 5-9. Just as Congress cannot create so many exceptions to the Supreme Court's jurisdiction as to destroy the Court's essential role in the constitutional plan, *see generally* Hart, *The Power of Congress to Limit the Jurisdiction of Federal Courts: An Exercise in Dialectic,* 66 HARV. L. REV. 1362 (1953), a state legislature cannot reserve so much power as to render the Contract Clause a nullity. Moreover, just as political pressures make it unlikely that Congress will enact broad exceptions to the Supreme Court's jurisdiction, similar pressures make it unlikely that a state legislature would enact a reservation statute permitting the modification of all statutes. Our constitutional jurisprudence should focus on situations that are likely to arise rather than on extravagant possibilities that the realities of our polity render remote.

140. For Professor Epstein's discussion of these examples, see Epstein, *supra* note 136, at 725-26.

legislation.[141] Conversely, because prospective legislation will affect a more diverse group of factions, there is more reason to believe that the legislative process will strike a proper balance between economic liberties and the protection of the needs of the general welfare.

Moreover, Professor Epstein's proposed rule of protecting expectations premised on prospective agreements would be difficult to apply and would be so expansive as to be inconsistent with the structure of federalism that underlies the Constitution. Since all legislation affects expectations, indulging Professor Epstein's interpretation of the Clause would permit federal judicial review of the substantive merits of almost all state enactments and would invite the federal judiciary to determine whether a state's interest underlying legislation is sufficient to defeat inchoate expectations.[142] In short, the error in Professor Epstein's analysis is his assumption that because the Framers were concerned about legislation that redistributed wealth at the expense of a minority, they were willing to structure the polity in such a way as to negate the risk of all such legislation, even at the cost of eviscerating other values such as representative government and federalism.

## Conclusion

Two important lessons may be drawn from this survey of contract clause history. The first is that the Supreme Court is more likely to decide cases according to neutral principles when the Court remains faithful to the original meaning of the Clause. It is ironic that the Supreme Court has chosen to apply the Contract Clause by balancing social interests in the manner of the legislature when the intent of the Clause was to forbid legislatures from retrospectively interfering with contracts. It is equally ironic that the Supreme Court has interpreted a constitutional provision that was designed to provide certainty to contracting parties in a manner that maximizes the unpredictability of its application. The genius of the Framers was that they formulated a provision which advanced the rule of law by minimizing the amount of balancing of

141. We have already noted that the Framers were particularly concerned with protecting a minority faction when it was likely that the faction would be isolated. *See supra* notes 16-18 and accompanying text.

142. Because under Professor Epstein's theory of the Clause all state legislation would be potentially subject to its strictures, courts would necessarily have to engage in a significant amount of balancing in order to decide which legislation was sufficiently justified by health or safety considerations to be upheld. This kind of jurisprudence transforms the Court into a kind of super legislature, which we believe is fundamentally inconsistent with the Court's function under the separation of powers.

interests that is contrary both to the purpose of the provision and the judicial function.

Our review of the Clause also underscores the importance of construing constitutional provisions in light of those concepts which the Framers viewed as fundamental to the preservation of liberty in a civil society. Two of these concepts—the separation of powers and federalism—are familiar. The rule of law and the prevention of the oppression of interests of minority factions may be less familiar, but equally deserving of serious consideration.

Besides contributing to the preservation of liberty through adherence to the rule of law, the original understanding of the Contract Clause serves as a principled demarcation between substantive due process and the judicial abnegation of review over economic legislation. The Contract Clause does not license the judiciary to prevent economic or social policies from ultimately being instituted by the legislative branch. States may pass legislation that greatly restricts the ability to make particular contracts in the future. However, the Contract Clause does secure from legislative impairment those enterprises in which a citizen is currently engaged and in which he or she possesses vested, tangible rights. The Contract Clause slows democratic change in social organization and distribution, but it does not preclude it. In the end, a return to the original understanding of the Contract Clause would permit an open, democratic future while respecting essential rights that have been acquired under the democratically enacted laws of the past.