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REVIVAL OR REVOLUTION: *U.S. TRUST*'S ROLE IN THE CONTRACTS CLAUSE CIRCUIT SPLIT

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The Contracts Clause[1] of the United States Constitution is one of the only protections against state interference with contractual obligations.[2] The Clause, adopted to restore the sanctity of contracts and stabilize commercial markets, was once a forceful weapon against state power.[3] However, decade after decade of exceptions nearly exiled the doctrine into constitutional anonymity.[4] The Supreme Court attempted to revitalize the doctrine in the 1970s, but instead only muddled the application of the Clause and left questions about its proper role.[5]

As it stands today, the Contracts Clause is a recurring source of confusion and ambiguity. Litigants are unsure of the scope of the Clause's power, and the circuits are equally uncertain of the true effect the Clause deserves. The Contracts Clause violation test is now the subject of a circuit split that has spawned varying approaches and conflicting interpretations.

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[1] The Contracts Clause states,

> 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.

U.S. CONST. art. I, § 10, cl. 1 (emphasis added).

[2] Contracts Clause jurisprudence reveals two different names used to refer to the clause: the "Contract Clause" and the "Contracts Clause." For the sake of uniformity and consistency, this Note refers to the provision as the "Contracts Clause."

[3] BENJAMIN FLETCHER WRIGHT, JR., THE CONTRACT CLAUSE OF THE CONSTITUTION xiii (1938).

[4] James W. Ely Jr., *Whatever Happened to the Contract Clause?*, 4 CHARLESTON L. REV. 371, 376 (2010).

[5] Thomas W. Merrill, *Public Contracts, Private Contracts, and the Transformation of the Constitutional Order*, 37 CASE W. RES. L. REV. 597, 598–99 (1987).

This split is best explained by the Supreme Court's failure to communicate a clear violations test in *U.S. Trust Co. of New York v. New Jersey*.[6]

U.S. Trust was supposed to be the savior of the Contracts Clause, breathing new life into the feeble doctrine and restoring it to its past glory.[7] Instead, the holes and ambiguities created by *U.S. Trust* have left the circuits wondering about the Clause's proper place, and have allowed courts to fill these holes with their own views of the Clause's power. *U.S. Trust*'s failure to adequately define the proper role of the Contract Clause has left the circuits with too little guidance and too much discretion. This ill-fated combination has allowed the courts to construct individual interpretations that have generated the circuit split before us today.

This Note argues that *U.S. Trust*'s Contracts Clause test created ambiguities that have spawned varying and conflicting approaches in the circuits. This Note also argues that *U.S. Trust*'s failure to advance the Framers' original intent and departure from precedent has created the doctrinal disagreement that feeds the circuit split. Part I presents the history of the Contracts Clause from the Constitutional Convention up to the decision in *U.S. Trust*.[8] Part II emphasizes the negative consequences of *U.S. Trust*'s novel approach by detailing the varying approaches the circuits have taken in applying the ambiguous dual standards set out in *U.S. Trust*. Part III critically analyzes *U.S. Trust*'s new violations standard and argues the Supreme Court needs to resolve the circuit split by reformulating *U.S. Trust*'s test. This Part then offers a new test that will clarify *U.S. Trust*'s ambiguities and correct its flaws.

I. CONTRACTS CLAUSE JURISPRUDENCE

The history of the Contracts Clause can be divided into four periods. The first period includes the introduction of the Contract Clause at the Constitutional Convention and its early interpretation by the Supreme Court.[9] The second period includes the circumstances leading up to the "death" of the Contracts Clause, illustrating the slow decline of its once robust

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[6] 431 U.S. 1 (1977).

[7] *See* Merrill, *supra* note 5, at 607–08.

[8] *See infra* Part I.

[9] *See infra* Part I.A.

power.[10] The third period includes the death of the Contracts Clause at the hands of the Supreme Court.[11] The fourth and final period centers on the Supreme Court's decision in *U.S. Trust* and its revival of the lifeless Contracts Clause.[12]

A. The Formation and the Early Years

The Clause's original task was to restore stability, prospectivity, and sanctity to contracts by preventing the states from interfering with private contractual obligations.[13] The need for such protection arose from the barrage of state legislation aimed at debtor-creditor relations following the Revolutionary War.[14] States continually passed legislation that freed debtors from their debts or denied creditors the means to enforce their liens.[15] When the failures of the Articles of Confederation forced the Framers to convene and develop the Constitution, the development of the Contracts Clause was set in motion.[16]

The Contracts Clause was originally based on the Northwestern Ordinance of 1787 ("Northwest Ordinance").[17] Although the Northwest Ordinance was limited to state interference with private contracts, the Framers eschewed any reference to "private contracts" in the Clause.[18] Because the

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[10] *See infra* Part I.B.

[11] *See infra* Part I.C.

[12] *See infra* Part I.D. This Note does not analyze or discuss any of the various Supreme Court decisions after *U.S. Trust*, because *U.S. Trust* was the last Supreme Court decision to deal with a public contract impairment. Although there have been numerous Supreme Court decisions regarding private contracts, they are not analyzed here mainly because the circuit court cases involved in the circuit split naturally have involved public contracts and thus have not relied on these private contract cases.

[13] Ely Jr., *supra* note 4, at 372.

[14] *Id.*

[15] *See id.*; *see also* Douglas W. Kmiec & John O. McGinnis, *The Contract Clause: A Return to the Original Understanding*, 14 HASTINGS CONST. L.Q. 525, 533 (1987).

[16] *See* Ely Jr., *supra* note 4, at 372–73.

[17] "[N]o 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." NORTHWEST ORDINANCE OF 1787 art. II (1787); *see also* Merrill, *supra* note 5, at 600.

[18] *See* Kmiec & McGinnis, *supra* note 15, at 530–32 (discussing the Framers' intent for the Clause to touch private and public contracts, unlike the Northwest Ordinance). It is speculated, however, that the Framers still believed the Clause only addressed private contracts. Some commentators argue that the lack of debate over the Clause shows that the Clause was not aimed at a state's own obligations, as the repayment of the states' mounting debt was a hot-button issue and if state

Clause received very little debate during the ratification process, its true meaning is not clear.[19] While the ratification process shed little light on the explicit meaning of the Contracts Clause, the Supreme Court gladly filled these ambiguities with its own interpretations.

The Marshall Court first interpreted the Clause and marked the apex of the Clause's power. During Chief Justice Marshall's tenure, the Clause became a "muscular restraint on state authority."[20] Chief Justice Taney continued to augment the Clause's power, but also narrowed its scope.[21] Taney "vigorously applied" the Clause to debtor-relief laws, state tax exemptions, and bond repudiations, but conversely afforded the states greater freedom to set economic policy.[22] This leeway given to the states to set economic policy marked the onset of the steady reduction of the Clause's power, as the Court would continue to carve out exceptions to the doctrine.

The trend toward carving out exceptions began in *Ogden v. Saunders*[23] and continued steadily on afterwards. In *Ogden*, the Court held that the State could impair contracts only if the impairment occurred prospectively, not retrospectively.[24] The majority found that the inclusion of the Clause alongside ex post facto laws[25] and bills of attainder[26] implied that the Clause was meant to protect existing rights only.[27] This greatly limited the scope of the Contracts Clause, as it now only protected actual contractual obligations, not the "right" to contract.[28] This limitation solidified the end of the expansion of the Clause's power and ushered in the era of the Clause's decline.

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representatives believed the Clause would address the issue, there certainly would have been more vocal debate over the Clause. *See* Merrill, *supra* note 5, at 600–01.

[19] Merrill, *supra* note 5, at 600.

[20] Ely Jr., *supra* note 4, at 374.

[21] *Id.*

[22] *Id.* at 374–75.

[23] 25 U.S. 213 (1827).

[24] *See id.* at 262.

[25] U.S. CONST. art. I, § 10, cl. 1.

[26] *Id.*

[27] *Ogden*, 25 U.S. at 286.

[28] Kmiec & McGinnis, *supra* note 15, at 537–38.

B. The Slow Decline

The slow ebb of the Contracts Clause's power began in *Ogden* and was expedited by *West River Bridge Co. v. Dix*.[29] There, the Court found that some state power was beyond the reach of the Clause, as "every contract is made in subordination to [the state right of eminent domain]."[30] The Court reasoned that the power of eminent domain was written into all contracts, as it is "superinduced by the preexisting and higher authority of the laws of nature, of nations, or of the community."[31] Eminent domain was the first power deemed beyond the reach of Contracts Clause review, but it would not be the last power put into this category.

The Court dealt another blow to the Clause's power in *Stone v. Mississippi*.[32] The Court created an exception for a state's police power, holding that a state could not contract away its power to protect society's health and morals; any attempt to do so would render the contract void.[33] This holding created what would become the reserved powers doctrine.[34] This doctrine held

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[29] 47 U.S. 507 (1848).

[30] *Id.* at 532–33.

[31] *Id.*

[32] 101 U.S. 814 (1879).

[33] *Id.* at 819.

[34] The reserved powers doctrine is sometimes used interchangeably with the inalienability doctrine. The inalienability doctrine stands for the proposition that a state legislature may not contract away certain powers. Although often used as synonyms, the two doctrines are technically different. There are multiple views of the differences between the two. One view is that the reserved powers doctrine falls within the inalienability doctrine, as "reserved powers" are always inalienable because they are written into every contract and cannot be contracted away. *See* Robert A. Graham, Note, *The Constitution, the Legislature, and Unfair Surprise: Toward a Reliance-Based Approach to the Contract Clause*, 92 MICH. L. REV. 398, 423, 427–28 (1993). A second view is that any difference between the reserved powers doctrine and inalienability doctrine is nominal. *See* Kmiec & McGinnis, *supra* note 15, at 546 n.101 ("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."). The third view is that the reserved powers doctrine applies to private contracts because these contracts are not made with the state, but these sovereign powers are "reserved" because they are an implied term in all contracts. *See* Note, *A Process-Oriented Approach to the Contract Clause*, 89 YALE L.J. 1623, 1626 (1980). The inalienable powers doctrine then applies only to public contracts, because there, a state actually obligates itself. *See id.* The state retains its sovereign powers here, but the powers are considered inalienable because the state cannot actually contract them away. *See id.* Because Contracts

that states had some sovereign powers that were "reserved" and could not be contracted away.[35] The Supreme Court increased the severity of this limitation in later decisions, as it continually expanded the scope of the states' police powers.[36] These exceptions greatly accelerated the decline of the Contracts Clause's power, as it now was insufficient to invalidate any state action taken in the name of public health or morals.[37]

By the mid-twentieth century, the Contracts Clause's decline was in full effect. Between 1941 and 1977, the Supreme Court did not invalidate any legislation under the Contracts Clause.[38] Furthermore, the Court, in *Manigault v. Springs*, extended the police power exception to private contracts.[39] The establishment of the emergency powers doctrine[40] further weakened the Clause, as the Court held that contracts were subordinate to the State's emergency powers.[41] The final blow came in *Home Building & Loan Ass'n v. Blaisdell*,[42] in which the Court further enlarged the police power exception to cover economic regulation.[43]

C. *The Death of the Clause*

The Court's decision in *Blaisdell* set the standard for a Contracts Clause violation test that stood for nearly forty years.[44] The Court held that although a literal interpretation of the

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Clause jurisprudence normally employs "reserved powers" as a blanket term for these doctrines, this Note uses the "reserved powers doctrine" to refer to the sovereign powers in both public and private contracts.

[35] *See* U.S. Trust Co. v. New Jersey, 431 U.S. 1, 23–24 (1977); Merrill, *supra* note 5, at 604–05.

[36] Michael L. Zigler, Note, *Takings Law and the Contract Clause: A Takings Law Approach to Legislative Modifications of Public Contracts*, 36 STAN. L. REV. 1447, 1452 (1984) ("Legislative actions . . . were upheld when the actions had been taken to abate nuisances, prevent lotteries, prevent the manufacture and sale of alcohol, and regulate railroad crossings. Thus the Court allowed the state to abrogate many public contracts in the pursuit of the public health, safety, and morals . . . ." (footnotes omitted)).

[37] *See id.*

[38] Ely Jr., *supra* note 4.

[39] 199 U.S. 473, 483 (1905); *see also* Ely Jr., *supra* note 4, at 387.

[40] For more on the emergency powers doctrine, see Roger I. Roots, *Government by Permanent Emergency: The Forgotten History of the New Deal Constitution*, 33 SUFFOLK U. L. REV. 259, 269–71 (2000).

[41] *See* Ely Jr., *supra* note 4, at 387–88 & nn.117–18.

[42] 290 U.S. 398 (1934).

[43] Ely Jr., *supra* note 4, at 389–90.

[44] Zigler, *supra* note 36, at 1454–55 (explaining the new standard set forth by U.S. Trust Co. v. New Jersey, 431 U.S. 1 (1977)).

Contracts Clause appeared to proscribe any impairment of contractual obligations, "the prohibition [was] not an absolute one and [was] not to be read with literal exactness like a mathematical formula."[45] This decision solidified the idea that the Contracts Clause does not invalidate all impairments of contracts.

The Court continued to assault the Clause in its reserved powers analysis. The Court held that a state "continues to possess authority to safeguard the vital interests of its people."[46] The Court reasoned that it did not matter if the legislation had "the result of modifying or abrogating contracts already in effect," as "the reservation of essential attributes of sovereign power is . . . read into contracts as a postulate of the legal order."[47] The Court rooted this reasoning in precedent, stating that the "principle of harmonizing the constitutional prohibition with the necessary residuum of state power has had progressive recognition in the decisions of this Court."[48]

The Court then explained how to apply the doctrine. A court first must ask "whether the legislation is addressed to a legitimate end and the measures taken are reasonable and appropriate to that end."[49] The Court then clarified this statement: "[T]he state power may be addressed directly to the prevention of the enforcement of contracts only when these are of a sort which the Legislature in its discretion may denounce as being in themselves hostile to public morals, or public health, safety, or welfare . . . ."[50] The Court limited the scope of this directive, stating the reserved powers doctrine does not allow "the state to adopt as its policy the repudiation of debts or the destruction of contracts or the denial of means to enforce them."[51]

In sum, *Blaisdell* held that a state may impair contracts under its reserved powers only when it seeks to prevent the enforcement of a contract that is hostile to public welfare or safety. *Blaisdell* did not address whether economic interests are included in the powers protecting the public welfare. The Court did find that "economic interests of the state may justify the

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[45] *Blaisdell*, 290 U.S. at 428.
[46] *Id.* at 434.
[47] *Id.* at 435.
[48] *Id.*
[49] *Id.* at 438.
[50] *Id.*
[51] *Id.* at 439.

exercise of its continuing and dominant protective power notwithstanding interference with contracts."[52] The Court, however, was dealing with an economic emergency in *Blaisdell*, thus narrowing the scope of its previous statement.[53] The Court also explicitly stated that the reserved powers could not be construed to allow a state to repudiate its debts.[54] *Blaisdell* did uphold the economic legislation at issue in the case, but the heavy focus on the emergency remedied left questions about the status of economic legislation under the reserved powers doctrine.

The impermanence of the legislation and the emergency it remedied were two of the five criteria *Blaisdell* relied on to uphold the State's act.[55] Another criterion was that the legislation had a legitimate purpose because it intended to protect the basic interests of society, not advantage specific individuals.[56] The third and fourth criteria supported the reasonableness of the act's relief.[57] Although *Blaisdell* initially was criticized,[58] it eventually became the standard for determining a Contracts Clause violation.[59]

The New Deal continued *Blaisdell*'s assault on the Contracts Clause. In reviewing actions taken under the New Deal, the Supreme Court afforded significant deference to state legislative judgments on economic policy and favored a broad regulatory power.[60] More importantly, the Supreme Court abandoned the principle that Contracts Clause exceptions were only applicable in emergencies.[61] The Contract Clause soon became "one of the banished provisions compromising the Constitution-in-exile,"[62] functioning as no more than " 'a pale shadow of its former self.' "[63]

Although the Contracts Clause would remain virtually dead-letter law until the *U.S. Trust* opinion, the Supreme Court's decisions after *Blaisdell* underscored the correct violations

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[52] *Id.* at 437.
[53] *Id.* at 444–45.
[54] *Id.* at 439.
[55] Kmiec & McGinnis, *supra* note 15, at 543.
[56] *Blaisdell*, 290 U.S. at 445.
[57] *Id.*; *see* Kmiec & McGinnis, *supra* note 15, at 543.
[58] Ely Jr., *supra* note 4, at 388–89.
[59] *Id.* at 388.
[60] *Id.* at 391.
[61] *Id.*
[62] *Id.* at 371.
[63] *Id.* (quoting Merrill, *supra* note 5, at 598).

standard. *City of El Paso v. Simmons*[64] dealt with a public contract impairment and elucidated the test required by *Blaisdell*. The Court cited *Blaisdell*'s rhetoric on the reserved power doctrine[65] and followed *Blaisdell*'s general approach.[66] Like the *Blaisdell* Court, the *El Paso* Court found no distinction between private and public contracts in its reserved powers analysis and did not communicate any dual deference standard.[67]

The precedent that the *El Paso* Court relied on for support is also significant. The *El Paso* Court's validation of the State's action was rooted in *East New York Savings Bank v. Hahn*'s[68] principle of respecting the wide discretion of a legislature.[69] *East New York* involved a private contract dispute,[70] yet the *El Paso* Court still relied on it in a public contract dispute.[71] Moreover, the *East New York* Court relied on the public contract analysis from *Blaisdell*[72] to assess the private contract impairment, but made no mention of a different analysis due to this disparity.[73] The fact that the Court assessed the Contracts Clause in *El Paso* and *East New York* with no regard to any public versus private distinction evidences the unified standard employed before *U.S. Trust*.

D. U.S. Trust *and the Revival of the Contracts Clause*

Roughly ten years after *El Paso*, the Supreme Court gave new life to the Contracts Clause in *United States Trust Co. v. New Jersey*.[74] *U.S. Trust* involved an impairment of a public contract: the repeal of a statutory covenant between New Jersey and holders of Port Authority bonds.[75] The Court quickly held that the State's repeal had impaired its contractual obligations,

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[64] 379 U.S. 497 (1965).

[65] *Id.* at 508 ("[T]he reservation of essential attributes of sovereign power is also read into contracts as a postulate of the legal order.").

[66] *El Paso* attempted to square the State's reserved powers with the impairment, evaluated the legislation's purpose, and assessed the means taken. *See id.* at 508–17.

[67] *See generally id.*

[68] 326 U.S. 230 (1945).

[69] *El Paso*, 379 U.S. at 508–09 (quoting *E. N.Y. Sav. Bank*, 326 U.S. at 232–33).

[70] *E. N.Y. Sav. Bank*, 326 U.S. at 232.

[71] *El Paso*, 379 U.S. at 498.

[72] 290 U.S. 398 (1934).

[73] *See generally E. N.Y. Sav. Bank*, 326 U.S. 230.

[74] 431 U.S. 1 (1977).

[75] *Id.* at 3, 9–10.

but found that an impairment alone was not enough for a violation, as courts must then ask if the impairment was constitutional.[76] The Court then reviewed the longstanding test to determine the constitutionality of an impairment, yet curiously adopted its own novel approach.[77]

The Court enunciated a two-prong test to assess an alleged violation of the Clause. First, was there a substantial impairment of contractual obligations?[78] Second, was this impairment constitutional?[79] This second prong involved two sub-inquiries: The Court first asked if a state's reserved powers were implicated, and then if the impairment was "reasonable and necessary to serve an important public purpose."[80] This novel approach included two vague dual standards that reduced the deference accorded to a state in a public contract impairment.[81] The Court employed the first of these dual standards in the reserved powers analysis, where it created two different approaches for public and private contracts.[82]

1. The Reserved Powers Analysis: Private Contracts

The Court began its dual approach to the reserved powers question by first addressing private contracts. The Court found that states "must possess broad power to adopt general regulatory measures without being concerned that private contracts will be impaired," as otherwise, a person could "obtain immunity from the state regulation by making private contractual arrangements."[83] The Court limited this broad power, however, when it held that "private contracts [were] not subject to unlimited modification under the police power."[84]

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[76] *Id.* at 21.

[77] *Id.* at 26–29.

[78] *Id.* at 17, 21.

[79] *Id.* at 21.

[80] *Id.* at 23, 25.

[81] *See id.* at 25–26 ("In applying this [reasonable and necessary] standard, however, complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State's self-interest is at stake.").

[82] *Id.* at 22–26.

[83] *Id.* at 22.

[84] *Id.* The Court does not explain why it only addresses the police power. The best explanation is that the police power has traditionally been considered implicit in every contract, and thus, must be addressed in every private contract analysis. *See, e.g.*, Manigault v. Springs, 199 U.S. 473, 480 (1905).

The Court then incorporated the *Blaisdell* standard into its reserved powers analysis. The Court found that legislation aimed at private contracts "must be upon reasonable conditions and of a character appropriate to the public purpose justifying its adoption."[85] The Court applied the *East New York* deference standard, holding that "[a]s is customary in reviewing economic and social regulation, . . . courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure."[86] In sum, under the reserved powers doctrine in a private contract,[87] the legislation must be reasonable and necessary to achieve a legitimate public purpose.[88] A court should also defer to the judgments of the legislature in its assessment of the above criteria.[89] The effect of this deference cannot be understated, as it effectively allowed the legislature to offer a defense for its legislation without fear of judicial scrutiny. The Court then analyzed public contract impairments under a different lens.

2. The Reserved Powers Analysis: Public Contracts

The Court created its first dual standard when it set forth a different analysis for the reserved powers doctrine in a public contract context.[90] The Court first defined the scope of the doctrine, finding that a state's police power and eminent domain power could "not be 'contracted away.' "[91] More importantly, the Court implied that the taxing and spending power was not a reserved power, as a state could unquestionably enter into

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[85] *U.S. Trust*, 431 U.S. at 22.

[86] *Id.* at 22–23. It is important to note that, in communicating this deference standard, the *U.S. Trust* court cited the *East New York* opinion's command for respect to the wide discretion of the legislature. *Id.*

[87] Although the *U.S. Trust* court never explicitly titled its analysis as the "reserved power doctrine for private contracts," this much is implied by its location in between the Court's general discourse on the reserved powers doctrine and the Court's explanation of the public contract reserved power doctrine. *See id.*

[88] *Id.*

[89] *Id.*

[90] The Court expressly created this dual standard when it held that "[w]hen a State impairs the obligation of its own contract, the reserved-powers doctrine has a different basis." *Id.* at 23.

[91] *Id.* This distinction highlights a nuance of the reserved power doctrine. In private contracts, the powers are an "implied term" because the state is not a party, while in public contracts, the power must actually be "contracted" away. *Id.* at 23–24.

financial contracts.[92] The Court then established a new standard of review for when a state does not contract away a reserved power.

The Court found that even though economic legislation did not fall under the reserved powers, the Contracts Clause was not an absolute bar to modification of a state's financial obligations. Instead, "[a]s with laws impairing the obligations of private contracts, [a public contract] impairment may be constitutional if it is reasonable and necessary to serve an important public purpose."[93] The Court provided no explanation for the shift from the "legitimate" public purpose for private contract impairments, to the "important" public purpose for public contracts.[94] After introducing a dual standard into the reserved powers analysis, the Court created another dual standard when it used a separate analysis for the deference question in public contract impairments.

In addressing the deference question for public contracts, the Court provided a standard different than the one employed for a private contract impairment. The Court held that public contract impairments did not deserve the deference accorded to private contract impairments, as "complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State's self-interest is at stake."[95] In effect, the Court filled in the opposite end of *East New York*'s respect for the legislature's discretion when evaluating an exercise of a reserved power[96]: When a reserved power was not implicated, complete deference was inappropriate. After the Court concluded its reserved powers analysis, it began its analysis of the "reasonable and necessary" prong.

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[92] *Id.* at 24. As the Court stated previously, the reserved powers doctrine barred the State from contracting away its police power or eminent domain power. *See supra* note 34.

[93] *U.S. Trust*, 431 U.S. at 25.

[94] *Id.* at 22, 25.

[95] *Id.* at 26.

[96] E. N.Y. Sav. Bank v. Hahn, 326 U.S. 230, 232–33 (1945) ("Once we are in this domain of the reserve power of a State we must respect the 'wide discretion on the part of the legislature in determining what is and what is not necessary.' " (quoting Manigault v. Springs, 199 U.S. 473, 480 (1905))).

3. The "Reasonable and Necessary" Prong

The Court divided the "necessary" requirement into two levels. First, the Court found that the State's "total" repeal of the covenant was not "essential," as "a less drastic modification" was feasible.[97] Second, the Court held that the State could have achieved its goal through alternative measures that would not impair its contract.[98] The Court explained that a state "is not completely free to consider impairing the obligations of its own contracts on a par with other policy alternatives" and cannot "impose a drastic impairment when an evident and more moderate course would serve its purposes equally well."[99] Thus, the Court found the impairment was not necessary and then evaluated the "reasonable" requirement.

The Court grounded its "reasonableness" analysis in the *El Paso* holding. The *El Paso* Court had elaborated on the "reasonable" standard from *Blaisdell* and evaluated the reasonable expectations of the contracting parties.[100] The *U.S. Trust* Court echoed *El Paso*'s rationale that had upheld an impairment because it was a "reasonable means to 'restrict a party to those gains reasonably to be expected from the contract' when it was adopted."[101] The *U.S. Trust* Court found the impairment here was not comparable to the one in the *El Paso* case because the "changes" addressed were of "degree and not of kind."[102] The Court thus implicitly defined "reasonable" as an impairment that restricts a party to the gains expected at the time of the contract.[103] Because the impairment was not reasonable or necessary, the Court held it violated the Contracts Clause.[104]

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[97] *U.S. Trust*, 431 U.S. at 29–30.

[98] *Id.* at 30.

[99] *Id.* at 30–31.

[100] City of El Paso v. Simmons, 379 U.S. 497, 514–15 (1965); *see U.S. Trust*, 431 U.S. at 31.

[101] *U.S. Trust*, 431 U.S. at 31 (quoting *El Paso*, 379 U.S. at 515).

[102] *Id.* at 32.

[103] *See id.* at 31–32.

[104] *Id.* This Note has not presented the *U.S. Trust* Court's discussion of the "public purpose," mainly due to the Court's cursory treatment of the purpose question. The Court quickly disposed of the question by finding that mass transit, energy conservation, and environmental protection were legitimate public interests. *Id.* at 28.

The successful Contracts Clause challenge in *U.S. Trust* represented a huge shift in the Clause's jurisprudence. The Court had reenergized the Clause and pulled it from the depths of constitutional anonymity. This revival, however, was not without criticism and resistance.[105] This resistance continues today, as some circuits have not wholeheartedly accepted the new challenger-friendly public contract approach and have sought to manipulate the test back to the traditional state-friendly approach.[106] Conversely, other circuits have zealously accepted the revival of the Clause and have used the *U.S. Trust* test as a harsh weapon against state action.[107] Finally, some circuits fall in between these two opposite approaches and employ their own, unique interpretation of *U.S. Trust*. These varying approaches have muddled the Contracts Clause landscape and have generated the current circuit split.

II. NEW LIFE AND NEW CONTROVERSY? THE CIRCUIT SPLIT OVER THE INTERPRETATION OF *U.S. TRUST*

The circuit courts have split over the interpretation of *U.S. Trust*'s violation test in two areas. First, the circuits have varied in their application of *U.S. Trust*'s "reasonable and necessary" prong, as some circuits have merged the prong with elements of past Contracts Clause standards, while other circuits have employed their own novel interpretations of the prong. Secondly, *U.S. Trust*'s dual standards have confused the lower courts, resulting in the emergence of varying, novel approaches to the deference question and reserved powers analysis. These two "splits" are exacerbated by the *U.S. Trust* Court's divergence from longstanding precedent, as the lower courts are unsure if they should base their tests upon the traditional "state-friendly" approach or attempt to apply their view of the "spirit" of *U.S. Trust*.

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[105] Justice Brennan authored a scathing dissent, in which he accused the majority of "reject[ing] [the] previous understanding and remold[ing] the Contract Clause into a potent instrument for overseeing important policy determinations of the state legislature" and "stand[ing] the Contract Clause completely on its head." *See id.* at 33, 53 (Brennan, J., dissenting).

[106] *See infra* Part II.A–B.

[107] *See id.*

A. *The Circuit Courts Have Split over the Application of the* U.S. Trust*'s "Reasonable and Necessary" Prong*

The Court's "reasonable and necessary" prong has spawned various, conflicting interpretations in the circuits. This conflict is rooted in both the Court's failure to explain its alterations to the traditional standard and failure to ground its new "necessary" requirement in precedent. This has left the circuits unsure if the *U.S. Trust* test discarded the previous standard or built upon it. As a result, lower courts have mixed elements of *U.S. Trust*'s standard with elements of the *Blaisdell* standard when applying the second prong. This "split" over the second prong has not produced two clear sides, but rather four varying approaches from just five circuits.

The Sixth Circuit, in *Toledo Area AFL-CIO Council v. Pizza*,[108] produced one varying approach to this second prong. The court's second prong blended principles of *U.S. Trust* with other Supreme Court precedent. The court held that a state must first proffer a "significant and legitimate" public purpose, and then the court must determine if "the adjustment of the 'rights and responsibilities of contracting parties [is based] upon reasonable conditions and [is] of a character appropriate to the public purpose justifying [the legislation's] adoption.' "[109]

This prong was not the correct "reasonable and necessary" standard from *U.S. Trust*, but instead was an amalgamation of the *Blaisdell* test and *U.S. Trust*'s second prong. The court retained the "reasonable" requirement from *U.S. Trust*, but replaced "necessary" with *Blaisdell*'s "appropriate" requirement.[110] The court seemed to use "necessity" and "appropriate" interchangeably throughout the opinion, despite the incongruence of these terms.[111] This unique test evidences the lower courts' uncertainty over which doctrinal principles to follow, as the Sixth Circuit blended the *U.S. Trust* and *Blaisdell* tests despite their inherent incongruities.

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[108] 154 F.3d 307 (6th Cir. 1998).

[109] *Id.* at 323 (alterations in original) (quoting Energy Reserves Grp., Inc. v. Kan. Power & Light Co., 459 U.S. 400, 412 (1983)).

[110] *See id.* This "appropriate" requirement was originally part of the *Blaisdell* test and was replaced with "necessary" by the court. *See infra* notes 170–71 and accompanying text.

[111] *See Toledo Area AFL-CIO Council*, 154 F.3d at 323, 325–27.

The second varying approach to the "reasonable and necessary" prong comes from the Fourth Circuit's opinion in *Baltimore Teachers Union v. Mayor of Baltimore*.[112] Here, the court proceeded as if it were applying *U.S. Trust*'s second prong, holding that "a government modification of its own financial obligations must be 'reasonable and necessary to serve an important public purpose.' "[113] The court continued to rely on *U.S. Trust*, finding that states must not " 'consider impairing the obligations of [their] own contracts on a par with other policy alternatives' or 'impose a drastic impairment when an evident and more moderate course would serve its purposes equally well,' nor act unreasonably 'in light of the surrounding circumstances.' "[114] Despite the court's recitation of the *U.S. Trust* rule, its application twisted the *U.S. Trust* test into a different approach.

The court found that since "the plan was less drastic than at least one alternative, additional layoffs, which could have been more detrimental," the State had not chosen a drastic impairment over a more moderate course.[115] This was a direct manipulation of the *U.S. Trust*'s "less drastic alternative" question under the necessary prong, as instead of determining if a *less* drastic course existed, the court upheld the impairment because a *more* drastic approach existed.[116] Thus, although the Fourth Circuit clothed its analysis in the language of *U.S. Trust*'s second prong, it ultimately twisted the test into its own novel approach that lowered the hurdle a state needed to clear to avoid invalidation.

The Ninth Circuit formulated its own version of the second prong in *Southern California Gas Co. v. City of Santa Ana*.[117] The court recited the "reasonable and necessary" language of *U.S. Trust*, but defined "reasonable" in a unique way.[118] The

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[112] 6 F.3d 1012 (4th Cir. 1993).

[113] *Id.* at 1018 (quoting U.S. Trust Co. v. New Jersey, 431 U.S. 1, 25 (1977)).

[114] *Id.* at 1020 (alteration in original) (citation omitted) (quoting *U.S. Trust*, 431 U.S. at 30–31).

[115] *Id.*

[116] *Compare id.* ("[T]he plan was less drastic than at least one alternative . . . ."), *with U.S. Trust*, 431 U.S. at 29–30 ("[I]t cannot be said that total repeal of the covenant was essential; a less drastic modification would have permitted the contemplated plan without entirely removing the covenant's limitations . . . .").

[117] 336 F.3d 885 (9th Cir. 2003) (per curiam).

[118] *See id.* at 894–96.

court held that an impairment is not reasonable if the impairment addresses a problem that existed at the time of the contract.[119] This interpretation warped *U.S. Trust*'s expectation approach, which found an impairment reasonable if it restricted a party to gains reasonably expected from the contract when it was adopted.[120] The Ninth Circuit's approach narrowed the scope of "reasonableness" to whether the problem addressed existed at the time of the contract and did not consider whether that problem produced unintended effects.[121] This unique variant on the second prong made it harder for a state to show its impairment was reasonable, thus, raising the hurdle to avoid invalidation.

The "reasonable and necessary" prong from the *U.S. Trust* decision has not been applied uniformly across the circuits. The circuits have produced four different tests because of the prong's open-ended nature. The Fourth, Sixth, and Ninth Circuits employ their own variation of the second prong, while the Second Circuit attempted to stay true to the *U.S. Trust* Court's original "reasonable and necessary" prong.[122] With four different approaches to *U.S. Trust*'s second prong circulating among the circuits, it is evident that the test's ambiguity and lack of guiding doctrinal support has confused the circuits.

B. The Circuit Courts Have Split in Their Interpretation of U.S. Trust*'s Dual Standards*

The *U.S. Trust* Court's dual deference standard and reserved powers analysis has sparked much more controversy among the circuits than its "reasonable and necessary prong." The root of these conflicting interpretations is the ambiguity and overall lack of guidance for lower courts on these two intertwined questions. Lower court interpretations of this test have shared two problems. First, many circuits routinely fail to even consider the reserved powers analysis and, thus, hinge the deference question on whether the impairment was public or private.[123] Second, the

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[119] *See id.* at 895.

[120] *See U.S. Trust*, 431 U.S. at 31.

[121] *See S. Cal. Gas Co.*, 336 F.3d at 894–96.

[122] In *Buffalo Teachers Federation v. Tobe*, the Second Circuit applied the "reasonable and necessary" prong with virtually no changes, and thus, that prong of the opinion is not discussed here. *See* 464 F.3d 362, 371–72 (2d Cir. 2006).

[123] *See infra* notes 128–30, 135, 137 and accompanying text.

lower courts have used the "less than complete deference" standard to apply very different levels of deference.[124] The vague and discretionary deference instruction has given rise to two divergent tests in the circuit courts.

1. The High Deference Approach

One approach to the *U.S. Trust* Court's deference instruction has been an interpretation favoring states. The First, Second, and Fourth Circuits have interpreted *U.S. Trust*'s "less deference" approach to conform with the "old" Contract Clause principles and afford states a great deal of deference.[125] These circuits have used this approach to warp the *U.S. Trust* decision into a test akin to the highly state-deferential *Blaisdell* test.[126]

The First Circuit twisted the *U.S. Trust* test into an approach highly deferential to the state in *UAW v. Fortuño*.[127] Dealing with a public contract impairment, the *Fortuño* court first erred when it gave only one sentence to the reserved powers doctrine, stating that a court must "reconcile the strictures of the Contracts Clause" with a states's sovereign power.[128] This statement was little more than lip service, as the court skipped the reserved powers analysis and instead applied the deference standard set aside for legislation not passed under reserved powers.[129] The court stated that "[w]here the state is alleged to have impaired a public contract to which it is a party, 'less deference to a legislative determination of reasonableness and necessity is required, because the State's self-interest is at stake.' "[130] The court then proceeded to clothe an approach highly deferential to the State in the language of *U.S. Trust*.

After reciting the *U.S. Trust* standard, the court injected its own subjective belief on the deference question under the guise of interpretation. The *Fortuño* court found that although "complete deference" to a legislature's findings was inappropriate under

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[124] *See Buffalo Teachers Fed'n*, 464 F.3d at 369; *see also infra* Parts II.B.1–2.

[125] *See infra* notes 133, 140, 146 and accompanying text.

[126] For a summary of the *Blaisdell* test, see *supra* Part I.C.

[127] 633 F.3d 37 (1st Cir. 2011).

[128] *Id.* at 41 (internal quotation marks omitted).

[129] This mere "lip service" is implied by the test employed by the court, which asked only whether there was an impairment and, if so, whether the impairment was reasonable and necessary. *See id.*

[130] *Id.* (quoting Parella v. Ret. Bd. of R.I. Emps.' Ret. Sys., 173 F.3d 46, 59 (1st Cir. 1999)).

U.S. Trust, "less than complete deference" certainly could not mean "no deference."[131] Furthermore, since legislative findings in private contracts are afforded substantially "heightened deference," a less deferential approach to public contracts must still yield "meaningful deference."[132] The *Fortuño* court exploited the ambiguity of the dual deference standard and effectively applied the *U.S. Trust* test with the state-friendly principles of pre-*U.S. Trust* Contracts Clause jurisprudence.[133]

The Second Circuit's interpretation of the *U.S. Trust* deference standard in *Buffalo Teachers Federation v. Tobe*[134] also favored the State. Just like the First Circuit, the *Tobe* court provided only a cursory reference to the reserved powers analysis, but failed to apply it.[135] Instead, the *Tobe* court divided the *U.S. Trust* Court's test into three prongs[136] and hinged the deference question on whether the impairment was public or private.[137] The court recognized that complete deference to the legislature in a public contract impairment was inappropriate, but reasoned that "less deference" does not equal "no deference."[138] The court reasoned that affording *no* deference to the State was the staple of heightened scrutiny review, and no Supreme Court decision warranted such a review.[139] The court then accorded significant deference to the State and held in its favor.[140] Just like the First Circuit, the Second Circuit twisted

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[131] *See id.* at 44.

[132] *See id.* at 44–45.

[133] For a discussion of the traditionally state-friendly principles of the Contracts Clause, see *supra* Part I.B–C.

[134] 464 F.3d 362 (2d Cir. 2006).

[135] The court referenced the reserved powers doctrine once, stating: "[The Contracts Clause] does not trump the police power of a state to protect the general welfare of its citizens . . . . [C]ourts must accommodate the Contract Clause with the inherent police power of the state." *Id.* at 367.

[136] *Id.* at 368. The other two prongs of the *Buffalo Teachers* test were (1) whether the contractual impairment was substantial and (2) whether "the law serve[d] a legitimate public purpose such as remedying a general social or economic problem." *Id.*

[137] *Id.* at 369 ("Public contracts are examined through a more discerning lens. When the state itself is a party to a contract, complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the [s]tate's self-interest is at stake." (alteration in original) (internal quotation marks omitted)).

[138] *Id.* at 370–71.

[139] *Id.* at 371. The court resisted heightened scrutiny, as "[s]uch a high level of judicial scrutiny of the legislature's actions would harken a dangerous return to the days of *Lochner v. New York*." *Id.*

[140] *Id.* at 370–72.

U.S. Trust's deference standard to reflect the traditional approach favoring deference to a state's justifications and thus contributed to the mounting circuit split.

The Fourth Circuit also took up a highly deferential approach in *Baltimore Teachers Union v. Mayor of Baltimore*.[141] The *Baltimore Teachers* court did a better job of addressing the reserved powers question, but still failed to apply it in the manner required by *U.S. Trust*. The court recited the language of the reserved powers doctrine[142] and correctly stated the doctrine's application to private contracts,[143] but inexplicably failed to apply the doctrine to the public contract at issue. Instead, the court placed the fulcrum of the deference standard on the public versus private distinction.

The *Baltimore Teachers* court let the public or private nature of the impairment control the level of deference accorded. A private contract would receive complete deference, while a public contract would stand on "a somewhat different footing" because the State's self-interest would be at stake.[144] The court then found that although "*complete* deference" was inappropriate, "some deference" must be accorded.[145] Although the court did not explain what "some deference" meant, it implicitly afforded the State a high level of deference when it upheld the legislation because it was unwilling to sit as a "superlegislature" and determine if a more appropriate action existed.[146] This approach unquestionably aligned with the First and Second Circuit's state-friendly interpretation of *U.S. Trust*.

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[141] 6 F.3d 1012 (4th Cir. 1993).

[142] The court recognized that it must "attempt to reconcile the strictures of the Contract Clause with the 'essential attributes of sovereign power' necessarily reserved by the States to safeguard the welfare of their citizens." *Id.* at 1018 (quoting U.S. Trust Co. v. New Jersey, 431 U.S. 1, 21 (1977)).

[143] "As where a government modifies a wholly private contract, a government modification of its own financial obligations must be 'reasonable and necessary to serve an important public purpose.'" *Id.* at 1018 (quoting *U.S. Trust*, 431 U.S. at 25).

[144] *Id.* at 1019.

[145] *Id.*

[146] *Id.* at 1021–22. "[E]ven where public contracts have been impaired [courts are not required] to sit as superlegislatures, determining, for example, whether it would have been more appropriate instead for Baltimore to close its schools for a week, an option actually considered but rejected, or to reduce funding to the arts . . . ." *Id.*

2. The Minimal Deference Approach

A second interpretation of the *U.S. Trust* deference standard favoring the challenger of the state action has also circulated among the circuits.[147] The Sixth and Ninth Circuits automatically applied *U.S. Trust*'s "less than complete" deference standard to all public contracts. These circuits have construed that instruction to mean minimal or no deference to the state legislature's assessments. Furthermore, they have ignored the traditional approach and constructed their tests to further what they believe is the "spirit" of *U.S. Trust*. This has resulted in the continued invalidation of state action under this hard-line Contracts Clause interpretation.

The Sixth Circuit aligned itself with this approach when it interpreted *U.S. Trust* to favor the challengers in *Toledo Area AFL-CIO Council v. Pizza*.[148] In analyzing a public contract impairment, the court claimed to incorporate the reserved powers doctrine, holding that the "essential attributes of sovereign power . . . necessarily reserved by the states to safeguard their citizens" were "recognized in the [Contracts Clause's] analytic framework."[149] Despite this statement, the court applied "less than complete deference" because a public contract was impaired, not because the legislative act fell outside of the reserved powers.[150]

Furthermore, the court offered a hard-line interpretation of *U.S. Trust*'s "less" deference standard, holding that the court would not blindly accept the State's proffered justifications as reasonable and necessary because the State's own self-interest was at stake.[151] Because of this self-interest, the court held it "must carefully scrutinize" the legislature's justifications and subsequently invalidated the State action.[152] Thus, the *Toledo* court effectively translated the "less than complete" deference command into a "careful scrutiny" standard that afforded minimal deference. This level of scrutiny took *U.S. Trust*'s

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[147] Unfortunately, these courts are not split from the other circuits in the failure to analyze the reserved powers, as all five of the circuits detailed here ignore the doctrine.

[148] 154 F.3d 307 (6th Cir. 1998).

[149] *Id.* at 323 (internal quotation marks omitted).

[150] *Id.* at 327.

[151] *Id.* at 325.

[152] *Id.* at 325–27.

standard to the extreme and is contrary to the First, Second, and Fourth Circuit's interpretation of *U.S. Trust*, as well as the state-friendly pre-*U.S. Trust* jurisprudence.[153]

The Ninth Circuit furthered the split over the *U.S. Trust* standard in *Southern California Gas Co. v. City of Santa Ana.*[154] Unlike the other circuits, the *Santa Ana* court did not even mention the reserved powers doctrine and ignored its role in determining the proper deference. The court's deference approach turned on the public versus private question, as it claimed that "a higher level of scrutiny" is required when "legislative interference involves a public rather than a private obligation."[155] The court then found that "[c]omplete deference . . . is not appropriate because the State's self-interest is at stake."[156] Although the court did not expressly state that low deference to a state's justifications was appropriate, it implied such throughout its analysis.

The court commented that since the State impaired its own contract, the State must bear the burden of proving its impairment was "reasonable and necessary."[157] The court described this burden as a "heavy burden" on the State.[158] The court proceeded to invalidate the State action because the justifications the State offered were not reasonable and not necessary.[159] Although the court's interpretation of *U.S. Trust* is less obvious, its imposition of a heavy burden on a state to justify its impairment is akin to affording minimal deference interpretation. The Ninth Circuit thus sides with the Sixth Circuit on the issue of deference, further deepening the circuit split.

The circuit courts have had trouble interpreting *U.S. Trust* and applying its violation test uniformly. This has led to varying interpretations and an expanding split among the circuits. The most alarming aspect of this split is that it has produced unique,

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[153] *See* UAW v. Fortuño, 633 F.3d 37 (1st Cir. 2011); Buffalo Teachers Fed'n v. Tobe, 464 F.3d 362 (2d Cir. 2006); Baltimore Teachers Union v. Mayor of Baltimore, 6 F.3d 1012 (4th Cir. 1993).

[154] 336 F.3d 885 (9th Cir. 2003).

[155] *Id.* at 889 (internal quotation marks omitted).

[156] *Id.* at 894 (internal quotation marks omitted).

[157] *Id.*

[158] *Id.* at 896.

[159] *Id.* at 896–97.

varying approaches in five different circuits.[160] The variance in these approaches highlights *U.S. Trust*'s lack of guidance and ambiguity. This Note argues that the *U.S. Trust* opinion has directly caused the split over the Contracts Clause violations test by promulgating a novel and ambiguous test that diverted from longstanding precedent and failed to further the Framers' intent. Thus, the Contracts Clause violations test must be reformulated into an unambiguous test that squares the *U.S. Trust* test with the traditional principles of Contracts Clause jurisprudence.

III. A REFORMULATED CONTRACTS CLAUSE VIOLATIONS STANDARD: THE THREE-PRONG TEST

The split that has emerged among these five Circuit Courts of Appeal displays the outcome of combining the ambiguity of the *U.S. Trust* decision with the Supreme Court's failure to adequately ground its decision in precedent or provide clear doctrinal support. The divergence from precedent and lack of doctrinal support has set the stage for conflict over the proper role of the Contracts Clause. The ambiguous and overly discretionary test communicated in *U.S. Trust* has enabled the circuits to air their subjective beliefs on this question. This undesirable mixture has muddled the *U.S. Trust* test and the Contracts Clause in general.

The Supreme Court should therefore reformulate the Contracts Clause violation test because it has become unworkable and has caused a split over the application of the test. The test has proven to be impracticable for three main reasons. First, the test fails to further the Framers' original intent.[161] Second, the *U.S. Trust* Court failed to reconcile the novel test with well-established precedent.[162] Third, the test is too ambiguous and thereby leaves too much discretion to the lower courts.[163] These three failures have combined to allow the circuits to proffer their own interpretations of the proper role of the Contracts Clause, thus generating a circuit split.

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[160] *See, e.g.*, UAW v. Fortuño, 633 F.3d 37 (1st Cir. 2011); Buffalo Teachers Fed'n v. Tobe, 464 F.3d 362 (2d Cir. 2006); S. Cal. Gas Co. v. City of Santa Ana, 336 F.3d 885 (9th Cir. 2003); Toledo Area AFL-CIO Council v. Pizza, 154 F.3d 307 (6th Cir. 1998); Baltimore Teachers Union v. Mayor of Baltimore, 6 F.3d 1012 (4th Cir. 1993).

[161] *See supra* Part I.A; *see also infra* Parts III.A.3–4.

[162] *See infra* Parts III.A.1–2.

[163] *See supra* Part II.B.

A. U.S. Trust: *A Critical Analysis*

The most apparent negative consequence of *U.S. Trust*'s holding—the circuit split—is rooted in the opinion's two overarching flaws. First, the overall ambiguity and the Court's failure to clearly express the new standards have given lower courts too much discretion in applying the test. The courts use this discretion to turn the test into a vehicle for their own subjective view on the proper role of the Clause. Second, the subjective views of the lower courts often clash due to the Court's failure to square the test with the Framers' original intent and 150 years of well-established precedent.[164] This has resulted in a split between courts that employ the test as a weapon against state action and courts that turn the test into a state-friendly analysis more akin to the *Blaisdell* standard.

The first problem arose when the *U.S. Trust* Court communicated a test that failed to further the Framers' original intent behind the Clause. The Framers intended the Clause to promote prospectivity and restore stability to contracts.[165] The *U.S. Trust* decision failed to stabilize contractual relations between states and private parties when it introduced a violations standard that gave lower courts significant discretion in assessing the constitutionality of an impairment.[166] This resulted in varying and conflicting approaches to the violations test. Furthermore, the Court failed to further the prospectivity of the contracts when it introduced vague standards susceptible to multiple, conflicting interpretations.[167] Although the effect of failing to further the Framers' intent is less tangible, the inconsistencies nonetheless have forced the lower courts to choose sides.

The second problem arose when the *U.S. Trust* Court introduced a completely novel approach to the Contracts Clause and turned nearly 150 years of well-established precedent on its head. Although the Court was well within its power when it reformulated the Contracts Clause violations test, its failure to address the traditional principles and precedent left lower courts with questions about the true meaning of the *U.S. Trust* test.[168]

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[164] *See supra* Parts I.A–C., II.A.
[165] *See supra* notes 13–20 and accompanying text.
[166] *See supra* Part I.D.1–3.
[167] *See supra* Part II.B.
[168] *See supra* Part II.

This departure from precedent split the lower courts into two conflicting sides: The courts agreeing with the modern, stronger Contracts Clause, and the courts loyal to the traditional state-friendly, weak Clause.

1. *U.S. Trust* Diverged from Precedent with Its Second Prong

The Court diverged from well-established Contracts Clause precedent when it altered the language of the *Blaisdell* "reasonable and appropriate" standard. The Court made two significant alterations to the then-current violations test. The first was the change of the modifier before "public purpose" from "legitimate" to "important."[169] This alteration significantly increased the hurdle a state must clear to avoid invalidation. The Court did not explain this change and provided no support for the change, despite the fact that a state now had to show its public purpose was not just genuine but also important. This modification was too significant to be left unexplained and unsupported, as it significantly increased a court's discretion in deciding the validity of a state's purpose and allowed it to evaluate the importance of that purpose.

The second alteration was the requirement that the impairment be "necessary" to attain "an important public purpose," instead of just "appropriate."[170] The effect of the "necessary" requirement as opposed to the "appropriate" requirement was significant, as it increased the difficulty of defending a Contracts Clause challenge. This shift meant that a state was now required to show that the impairment was virtually its *only* choice, instead of just having to show that the impairment was a *suitable* choice under the old *Blaisdell* standard.[171] Despite these harsh effects, the Court again did not explain why it was raising a state's hurdle for constitutionality.

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[169] *Compare* U.S. Trust Co. v. New Jersey, 431 U.S. 1, 25 (1977), *with* Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 438–39 (1934).

[170] *Compare U.S. Trust*, 431 U.S. at 25, *with Blaisdell*, 290 U.S. at 438.

[171] Furthermore "appropriate" usually denotes a minimal scrutiny standard that is highly deferential to the legislature's assessments. *See U.S. Trust*, 431 U.S. at 54 n.17 (Brennan, J., dissenting) ("Reasonableness generally has signified the most relaxed regime of judicial inquiry."); Kmiec & McGinnis, *supra* note 15, at 546 ("A reasonableness test is a fairly relaxed or minimal standard of constitutional review . . . ."). Conversely, "necessary" denotes a heightened scrutiny standard that affords almost no deference to the legislature's justifications. *See U.S. Trust*, 431 U.S. at 54 n.17 ("[T]he element of necessity traditionally has played a key role in the most penetrating mode of constitutional review."); Kmiec & McGinnis, *supra* note

More alarmingly, the Court failed to provide relevant precedential support for this significant divergence from *Blaisdell*. The Court supported its new "necessary" requirement with one citation to *City of El Paso v. Simmons* that failed to support its assertion.[172] The *El Paso* Court did not require the legislation to be "necessary" to be constitutional; it only found that the legislation was constitutional *because* it was necessary.[173] The *U.S. Trust* Court's sole reliance on *El Paso* was thus unfounded, and only further weakened the doctrinal support behind its new second prong.

Although the *U.S. Trust* Court only made two alterations to the *Blaisdell* standard, these two alterations had resounding effects on the Contracts Clause test. Most importantly, the changes turned the state-friendly *Blaisdell* test into a potent weapon against state action. This radical doctrinal shift left lower courts confused over the principles underlying the test, leading to conflicting approaches among the circuits. Unfortunately, the *U.S. Trust* decision initiated another shift from precedent when it created two dual standards separating public contracts from private contracts.

2. *U.S. Trust* Diverted from Precedent with Its Dual Standard

U.S. Trust's introduction of the two dual standards that split the reserved powers analysis and deference question flipped nearly 150 years of precedent on its head. The Court departed from precedent in this context in two ways. First, the Court's two dual standards ignored the traditional approach of a unified analysis for both public and private contracts. Second, the dual standards protected public contracts more than private contracts despite the Court's established tradition of carving out exceptions to *decrease* protection for public contracts.

15, at 546 (stating that "formulations employing necessity have been viewed as calling forth a more exacting standard.").

[172] *See U.S. Trust*, 431 U.S. at 30–32 (majority opinion).

[173] *See* City of El Paso v. Simmons, 379 U.S. 497, 516–17 (1965) ("[A] statute of repose was quite clearly necessary . . . . The Contract Clause does not forbid such a measure.").

a. Precedent Calls for a Single Approach to Both Public and Private Contract Impairments

The traditional violations test employed one standard for both public and private contract impairments. Support for this idea can be traced all the way back to the Marshall Court's seminal decision in *Fletcher v. Peck*.[174] In that public contract dispute, Marshall expressly stated that the Contracts Clause protected public and private contracts equally.[175] The Court rooted its holding in the Constitution, finding that the language of the Clause drew no distinction between public and private contracts.[176] The *U.S. Trust* Court thus rebuffed the Marshall Court's vision of the Clause when it installed a dual standard distinguishing private contracts from public contracts.

The Supreme Court's decisions prior to *U.S. Trust* also support a unitary approach.[177] First, the *Blaisdell* decision offered a violations test without any regard to the public or private nature of the contract and rooted this approach in a great deal of precedent. The *Blaisdell* Court undertook an exhaustive review of Contracts Clause jurisprudence yet found no difference in the analysis of public and private contracts.[178] More specifically, the Court explicitly held that the reserved powers were read "into all contracts, *whether made between states and individuals or between individuals only*."[179] Furthermore, the Court continued to support its analysis with both public and private contract cases without noting any distinction.[180]

The Supreme Court's later decisions interpreting *Blaisdell* provide more support for a single standard. The Court first interpreted *Blaisdell* in *East New York Savings Bank v. Hahn*.[181]

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[174] 10 U.S. 87 (1810).

[175] *Id.* at 137–39.

[176] *Id.*; Merrill, *supra* note 5, at 603.

[177] There is a significant amount of precedent between the *Fletcher* decision and the *Blaisdell* opinion. Presenting a summary of this jurisprudence would be an exercise in redundancy, as *Blaisdell* exhaustively reviewed the vast body of Contracts Clause law before describing its test. Thus, *Blaisdell*'s test is an adequate representation of this history. *See generally* Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 427–42 (1934).

[178] *See id.*

[179] *Id.* at 435 (emphasis added) (quoting Long Island Water Supply Co. v. City of Brooklyn, 166 U.S. 685, 692 (1897)) (internal quotation marks omitted).

[180] For an example of the private contract precedent cited, see *id.* at 437 (citing to Manigault v. Springs, 199 U.S. 473 (1905)).

[181] 326 U.S. 230 (1945).

East New York was a private contract dispute, yet the Court fully relied on *Blaisdell*—a public contract dispute—without any mention of a dual standard.[182] Secondly, the Court in *City of El Paso v. Simmons*[183] relied on both *Blaisdell* and *East New York* for support, yet made no mention of a public versus private disparity.[184] These opinions made no indication of any dual standard for the reserved powers analysis or the deference analysis. Thus, the *U.S. Trust* Court offered an approach never before seen in Contracts Clause jurisprudence when it separated the reserved powers and deference analyses for public contracts from the private contract analysis.[185]

The *U.S. Trust* Court effectively admitted there was no precedential support for its dual standards when it relied on Fifth Amendment cases for support. The Court relied most on the *Gold Clause*[186] case of *Perry v. United States*,[187] which imposed an analogous dual standard in a dissimilar context.[188] The *Perry* case was a Fifth Amendment case, not a Contracts Clause case, and thus concerned contractual rights with the federal government.[189] Furthermore, the *Perry* Court used a dual standard of review for federal legislation abrogating contractual gold clauses.[190] More importantly, the Supreme Court completely

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[182] *Id.* at 230–32.

[183] 379 U.S. 497 (1965).

[184] *Id.* at 508–09.

[185] This is not to say there have never been any dual standards implemented by the Supreme Court. The Court once created an implicit dual standard that required public contracts to be construed narrowly and against the challenger, while private contracts were to be construed normally. *See* Charles River Bridge v. Warren Bridge, 36 U.S. 420, 544 (1837); Merrill, *supra* note 5, at 604.

[186] The *Gold Clause* cases were a series of decisions surrounding President Roosevelt's joint resolution that declared all contracts requiring the payment of obligations in gold to be against public policy. *See* Merrill, *supra* note 5, at 605–06.

[187] 294 U.S. 330 (1935).

[188] *See* U.S. Trust Co. v. New Jersey, 431 U.S. 1, 26 n.25 (1977) (citing *Perry*, 294 U.S. at 350–51; Norman v. Balt. & Ohio R.R., 294 U.S. 240, 304–05 (1935); Lynch v. United States, 292 U.S. 571, 580 (1934)).

[189] *See* Merrill, *supra* note 5, at 607 (explaining that the *Gold Clause* cases, which *Perry* is considered a part of, were decided under the Fifth Amendment). Furthermore, the Supreme Court has never "incorporated" the Contracts Clause into the Fifth Amendment. *Id.*

[190] *See generally Perry*, 294 U.S. 330 (finding that the plaintiff's claim of a constitutional violation arose due to a joint resolution of Congress); Merrill, *supra* note 5, at 606–07 (stating that the Court "drew a sharp distinction between the application of the joint resolution to contractual obligations of private corporations and state and municipal governments, and the application of the resolution to the obligations of the United States").

ignored *Perry* when deciding a public contract impairment in *El Paso v. Simmons*,[191] which was decided twenty years after *Perry*.[192] The *El Paso* Court applied the *Blaisdell* principles and did not even mention *Perry*'s dual standard.[193] Thus, the *U.S. Trust* Court grounded its support for its dual standard in a dissimilar and inapplicable case that the Court had ignored in previous Contract Clause cases.

The *U.S. Trust* Court also cited to *Lynch v. United States*,[194] to support its new dual standard. The *Lynch* decision, however, similarly fails to provide any support for a dual standard.[195] *Lynch* was a contract action against the federal government.[196] Although *Lynch* deals with the abrogation of contracts to lessen government expenditure, it involves *congressional* spending, not state expenditure.[197] Because of this distinction, the case does not contemplate the relationship between a state's spending power and reserved powers. This dissimilarity diminishes any support *Lynch* provided for the *U.S. Trust* Court's dual deference standard. The lack of precedential support in *U.S. Trust* is even more troubling in light of the Supreme Court's well-established and contrary trend of creating exceptions to favor the states.

b. Contracts Clause Exceptions Traditionally Favor the State, Not the Challenger

The Court flouted its long tradition of creating exceptions[198] to favor the state when it created a novel dual standard that scrutinized public impairments more harshly than private impairments. The first evidence of this trend came in *Charles*

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[191] *See* City of El Paso v. Simmons, 379 U.S. 497 (1965).

[192] Perhaps more revealing of *Perry*'s inapplicability is the fact that *Perry* and *Blaisdell* were decided only a year apart, yet the *El Paso* Court relied on *Blaisdell* but not *Perry*.

[193] *See El Paso*, 379 U.S. at 507–08.

[194] 292 U.S. 571 (1934).

[195] U.S. Trust Co. v. New Jersey, 431 U.S. 1, 26 n.25 (1977).

[196] *Lynch*, 292 U.S. at 575.

[197] *Id.* at 580 ("But Congress was without power to reduce expenditures by abrogating contractual obligations of the United States.").

[198] The Author will refer to any advantage given to one side in the clause's test as an exception. Although the dual standard from *U.S. Trust* is not an "exception" in the general sense, it is advantageous to the challenger and will be referred to as an exception. This is done to avoid the confusing problem of having "dual" dual standards: one set of "dual standards" that differentiate between public contracts and private contracts and another set of "dual" standards that favor challenger over the state or vice versa.

River Bridge v. Warren Bridge.[199] There, the Court interpreted the exclusivity of a public covenant.[200] Taney construed the covenant in favor of the State, holding that "any ambiguity in the terms of the contract, must operate against the adventurers, *and in favor of the public*, and the plaintiffs can claim nothing that is not clearly given them by the act."[201] *Charles River Bridge* created the core Contracts Clause principle that courts were to strictly construe public contracts in favor of the states. [202] This holding marked the onset of a long line of exceptions favoring the states.

The most powerful of these exceptions favoring the states is found in *West River Bridge Co. v. Dix.* [203] In *West River Bridge*, the Supreme Court created the oft-cited reserved powers doctrine.[204] The Court used the doctrine to exclude the State's eminent domain power from the Clause's grasp, as the power would be considered either an implied contract term or the contract would be invalid *ab initio* because it bound this power.[205] This holding created an exception that favored the states, as they could now exercise their eminent domain power without fear of impairment.

The states would benefit even more when the Court added the police power to this doctrine. In *Stone v. Mississippi*, the Supreme Court held that the State's police power—or the power over health and morals—was a sovereign power that the State could not bargain away.[206] The Supreme Court continually

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[199] 36 U.S. 420 (1837).

[200] *See id.* at 421 (stating that the plaintiffs claimed right to construct bridges granted by the Massachusetts legislature was exclusive). For more on Chief Justice Taney and the Contracts Clause, see Ely Jr., *supra* note 4, at 374–75.

[201] *Charles River Bridge*, 36 U.S. at 544 (emphasis added) (internal quotation marks omitted).

[202] Merrill, *supra* note 5, at 604. Although this principle of construction operates as a dual standard in some ways, it was not raised by *U.S. Trust* and is rarely disputed.

[203] 47 U.S. 507 (1848).

[204] *See, e.g.*, Zigler, *supra* note 36, at 1451–53.

[205] 47 U.S. at 532. Practically, the difference between these two methods of "escaping" review is subtle. A private contract would contain the reserved power as an "implied term," because the state was not a party to the contract. An exercise of the "implied" power would not be an impairment because it was "written" into the contract. A public contract would be invalid *ab initio* because the state contracted away a power it was unable to bind.

[206] 101 U.S. 814, 817 (1879). Later courts would clarify and expand this holding, finding that the police power was implicitly written into every contract as well. *See* Manigault v. Springs, 199 U.S. 473, 480 (1905).

expanded the scope of the state's police power, thus expanding the advantages of the exception.[207] The Supreme Court's addition of the police power to the reserved powers is another example of an exception to the Clause that favored the state.

The idea that exceptions usually favor the state is deeply ingrained in Contracts Clause jurisprudence. Thus, when the *U.S. Trust* Court adopted a test that did the exact opposite of this and installed a dual standard favoring the challenger with little explanation, the lower courts were understandably confused. Specifically, the circuits have been unsure if *U.S. Trust* has discarded the vast body of precedent that emphasized restraint when limiting a state's power and instead adopted an approach that affords much less deference to a legislature's assessments. Moreover, the *U.S. Trust* Court's failure to further the Framers' goals that underlined the Clause amplifies this uncertainty.

3. *U.S. Trust*'s Second Prong Fails To Further the Framers' Intent

Although the lack of debate over the Contracts Clause during ratification has created some uncertainty about the Framers' true intent,[208] the circumstances surrounding the Clause's adoption make at least two purposes clear. First, the Clause's adoption was an attempt to remedy the mounting creditor-debtor crisis and restore stability to both state and national markets.[209] Secondly, the Clause was meant to insulate private contracts from the whims of the majority and restore prospectivity to private contracting.[210] *U.S. Trust*'s second prong and dual deference standard failed to further either of these goals, as the abrupt change to the Contracts Clause landscape destroyed prospectivity and the overly discretionary test undermined stability.

The first problem with the second prong is that its "necessary" requirement does not advance the Framers' original goal to promote stability and prospectivity. For the "necessary"

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[207] *See* Zigler, *supra* note 36. ("Legislative actions abrogating state charters or other forms of public contracts were upheld when the actions had been taken to abate nuisances, prevent lotteries, prevent the manufacture and sale of alcohol, and regulate railroad crossings." (footnotes omitted)).

[208] *See* Merrill, *supra* note 5, at 600.

[209] Kmiec & McGinnis, *supra* note 15, at 529; *see supra* Part I.A.

[210] Kmiec & McGinnis, *supra* note 15, at 529.

question, the Court vaguely ordered that if a less drastic modification was available, the impairment was not necessary.[211] Second, if a state could have achieved its aim by taking alternative measures that would not impair the contract, the impairment was not necessary.[212] This standard does provide some vague outer limits, but leaves the lower courts with significant discretion in assessing "necessity." Courts are thus free to subjectively evaluate whether it believes an impairment was "more drastic" than need be, or if the ends of the impairment could have been achieved by "alternative" measures that would not impair the contract.

This format cannot promote stability of contracts or state markets. The Framers adopted the Contracts Clause to stop states from enacting individualized credit laws.[213] Thus the Framers could not have intended for the lower courts and each circuit to employ a unique Contracts Clause approach that was informed by their own subjective beliefs. These unique approaches would lead to the same inconsistent and unstable commercial market the Framers sought to remedy.

Furthermore, if courts are able to judge the "necessity" of an impairment based on their discretion and subjective beliefs, they essentially hold the power to make a contract worthless. Such a degree of discretion cannot promote prospectivity, as the parties will be unable to predict the outcome of a Contracts Clause challenge, and thus will not be able to rely on current contracts when planning future acts. The necessary prong of the *U.S. Trust* test does not meet the Framers' goal of stability and prospectivity as the actions, obligations, and expectations of both the state and private contracting parties will be left to the discretion of the Court.

4. *U.S. Trust*'s Dual Deference Standard Fails To Further the Framers' Intent

Similarly, *U.S. Trust*'s dual deference standard does not further the Framers' goal of preventing state interference with creditor-debtor contracts. The Framers intended for the Contracts Clause to preserve the sanctity of creditor-debtor

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[211] U.S. Trust Co. v. New Jersey, 431 U.S. 1, 29–30 (1977).

[212] *Id.*

[213] *See* Ely Jr., *supra* note 4, at 372.

contracts,[214] which are normally established through private contracts. It is thus safe to infer that the Framers aimed at least in part to provide equal—if not more—protection for private contracts than public contracts. A dual deference standard that protects private contracts less than public contracts cannot further this goal; it does not follow that the Framers would want to protect public contracts *more* than private contracts when they specifically adopted the Clause to prevent states from undermining private contracts.[215]

Moreover, the Contracts Clause was based on the Northwest Ordinance, which was aimed at private contracts, not public contracts.[216] The Framers deleted the "private contract" language and added the Clause with no distinction between public and private contracts.[217] The Framers' intentional deletion of "private" shows their desire for one standard; if the Framers wanted a dual standard, they would have left the term "private" in the Clause. Thus, the *U.S. Trust* Court ignored the Framers' intent when it set forth a dual standard for public and private contracts.

5. *U.S. Trust* Failed To Communicate a Clear and Well-Guided Contracts Clause Test

The final problem with the *U.S. Trust* opinion is its failure to express the new standard clearly enough to guide the circuits in their application of the test. This has combined with the two problems above to produce conflicting violation tests in the circuits. The lack of guidance allows the decision's inconsistency with precedent and the Framers' intent to become a problem, as courts have exploited the ambiguity to speak their views on the proper role of the Contracts Clause.

The dual deference standard is ambiguous and thus leaves too much discretion to lower courts. *U.S. Trust* orders that "complete deference" to a legislature is inappropriate in the public contract context, but fails to elucidate what level of deference is "appropriate."[218] Courts have exploited this failure and warped the test to provide the level of deference they see fit.

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[214] *See U.S. Trust*, 431 U.S. at 45.
[215] *See id.*
[216] *See supra* note 17.
[217] *See* Kmiec & McGinnis, *supra* note 15, at 530, 532.
[218] *U.S. Trust*, 431 U.S. at 26.

Some circuits have interpreted the deference standard to mean significant, but not quite complete, deference. These courts have stayed loyal to the tradition of restraint when limiting a state's power. Other courts have interpreted the deference standard to mean no deference at all. These circuits have pushed the "spirit" of *U.S. Trust*'s "less deference" approach to its outer limits. The ambiguity of the deference standard allowed these two conflicting interpretations to arise,

In sum, the *U.S. Trust* Court's failure to address precedent, to conform to the Framers' intent, and to clearly express its new Contracts Clause test has given lower courts too much leeway. The test has become a vehicle for the lower courts' subjective beliefs rather than the stabilizing force the Framers intended it to be. The open-ended and discretionary nature of the test has left it unworkable and necessitates the test's reformulation.

IV. THE REFORMULATED CONTRACTS CLAUSE VIOLATIONS TEST: A THREE PRONG APPROACH

This Note argues that the only remedy for the troubling circuit split is for the Supreme Court to clarify the holding of *U.S. Trust* and set forth a new, clear violations test. This test should not simply overturn *U.S. Trust*, but instead should attempt to clarify the Court's test and better square it with the Clause's deep-rooted jurisprudence. Additionally, the new test should not merely adopt one of the circuit court's interpretations, as each of the five circuit tests offers no improvement over the *U.S. Trust* test, and instead exacerbates its flaws.

The "state-friendly" approach of the First, Second, and Fourth Circuits is ill-advised because it leaves the Contracts Clause virtually powerless. This test employs a high deference standard similar to the standard from *Blaisdell*, but fails to retain *Blaisdell*'s "emergency" and "temporary" prongs, which served as protections of the Clause's power.[219] The test also manipulates the ambiguity of *U.S. Trust*'s deference standard[220] to allow the court to afford any level of deference short of

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[219] The *Blaisdell* Court upheld the State impairment, but partially due to its temporary nature and the existence of an emergency. The approach of the First, Second, and Fourth Circuits fails to include these two important factors. *See* Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 444–48 (1934).

[220] *See U.S. Trust*, 431 U.S. at 26 (finding that "complete deference to a legislative assessment . . . is not appropriate").

"complete deference."[221] The test is just as unworkable as the *U.S. Trust* test, as it interprets the *U.S. Trust* test's ambiguity with its own lack of clarity.

The Sixth and Ninth Circuit's "challenger-friendly" approach falls on the opposite end of the spectrum. These circuits mold the Contracts Clause into a harsh weapon against state action. The test exploits the ambiguity of the *U.S. Trust*'s "less than complete" deference standard and takes it to an extreme by affording almost no deference to the states' assessments.[222] This minimal deference level only magnifies *U.S. Trust*'s inconsistency with precedent, and thus the Supreme Court should not adopt this test.

Since both interpretations offered by the circuits are unworkable and intensify *U.S. Trust*'s flaws, the Supreme Court should provide a new test. This test will express the *U.S. Trust* test in more clear terms and better align the test with the Clause's established jurisprudence. The first prong will be the traditional threshold question: Was there a substantial impairment of contractual obligations? The second prong will require a reserved powers analysis, and the third prong will employ a three-part balancing approach assessing the constitutionality of the impairment.

Lastly, there is no deference standard in this test. This is because the deference standard was a construct of the *East New York* decision that the *U.S. Trust* Court distorted into a novel standard. *Blaisdell* and previous decisions did not apply any type of deference standard, thus the Court should not provide one here. The reserved powers doctrine will afford a state the necessary "deference," as the doctrine will prevent courts from interfering with a state's eminent domain or police powers. The proposed test was composed with an eye toward eliminating the deference question, and thus, the prongs attempt to pose factors that will not raise a debate over levels of deference and will remove most of the discretion present in the *U.S. Trust* test.

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[221] *See supra* Part II.A.2.

[222] Although neither the Sixth nor Ninth Circuit explicitly states such, the Sixth Circuit's requirement of "careful scrutiny" and the Ninth Circuit's imposition of a heavy burden clearly imply as much. *See supra* Parts II.B.2.

A. *The First Prong*

The first prong will present the Supreme Court's traditional threshold question: Was there an impairment of a contractual obligation?[223] This prong will exactly mirror the first prong of the *U.S. Trust* test.[224] As a threshold question, if this question is answered in the negative, the court will find no Contracts Clause violation. An affirmative answer will lead to the second prong.

B. *The Second Prong*

The second prong is a reserved powers analysis. Most importantly, this prong requires one reserved powers analysis for *both* public and private contracts. The prong will ask if the contract or impairment involves a reserved power of the states.[225] The eminent domain power and the police power will be included under these reserved powers. The police power will include the power to protect the health, safety, and morals of the public. There will be no violation if the court finds that the impairment occurred because a state had exercised a reserved power that it either contracted away or that was implied in the contract's terms.

Economic legislation, the taxing power, and the spending power do not fall under the protection of the reserved powers doctrine. The *Blaisdell* Court first brought up this concern when it held that a state cannot repudiate its debts or deny the means

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[223] Although there is some debate over whether this prong should require a "substantial impairment" or just a "technical impairment," this question is well beyond the scope of this Note and will not be addressed. For more on this debate, see *U.S. Trust*, 431 U.S. at 41 (Brennan, J., dissenting) ("[The majority's] consideration of the countervailing injury ostensibly suffered by the appellant is barely discernible at all. For the Court apparently holds that a mere technical impairment of contract suffices to subject New Jersey's repealer to serious judicial scrutiny and invalidation under the Contract Clause." (internal quotation marks omitted)); Zigler, *supra* note 36, at 1456, 1456 nn.54–56 ("Courts had long recognized that if the contract clause were read literally it would effectively prevent the state from enacting any legislation at all. Minimal impairments were therefore to be disregarded, and only substantial impairments were prohibited." (footnote omitted)).

[224] The prong mirrors *U.S. Trust*'s version because the merits and wisdom of the first prong are beyond the scope of this Note. Moreover, the first prong has generated virtually no controversy and has not contributed to the split.

[225] This prong looks to both the contract and impairment so it can adequately cover private and public contracts. In a private contract setting, the reserved power will almost always arise in the impairment, since the state was not a party to the contract. Alternatively, in the public contract, the state is more likely to have contracted away or obligated its reserved power.

to enforce them.[226] Furthermore, the *U.S. Trust* Court's skepticism of state legislation that alters the legislation's own financial obligations was well founded.[227] As the *U.S. Trust* Court wisely argued, the chance for legislative self-dealing increases when the state's financial obligation is involved, and the state will always have a need for extra money.[228] Thus, when the state passes legislation pursuant to a power outside of the "reserved" powers, the court will review the legislation objectively.[229]

C. The Third Prong

The third prong of this test will ask whether the impairment was constitutional. Since this question has been the prime source of confusion and misinterpretation, a five-part balancing test will be installed to determine the constitutionality of the impairment. To meet the goals of reducing the discretion afforded to the courts, eliminating the ambiguity of the test, and preventing subjective weighting, the five parts will all be held with equal weight. This creates an easy and clear procedure that prevents subjective manipulation: A court must find three of the factors to be in favor of constitutionality for the legislation to be upheld, and conversely, three factors must be found in favor of unconstitutionality for the legislation to the invalidated.

1. The First Factor

The first factor will ask if the impairment impinged on the reasonable expectations of the party. If this question is answered in the affirmative, then the factor supports the invalidity of the impairment. Naturally, if the answer is in the negative, then this factor swings in favor of constitutionality. Three sub-questions will help the lower courts answer this question and eliminate any ambiguity.

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[226] Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 439 (1934).

[227] *See U.S. Trust*, 431 U.S. at 26 (majority opinion) ("A governmental entity can always find a use for extra money, especially when taxes do not have to be raised. If a State could reduce its financial obligations whenever it wanted to spend the money for what it regarded as an important public purpose, the Contract Clause would provide no protection at all.").

[228] *Id.*

[229] Although this review seems to expose the legislation to "heightened scrutiny," the objective nature of the third prong will not disadvantage the legislature or set any presumption against the court's decision.

The first sub-inquiry will ask if the legislation prevented the party from obtaining a windfall. An answer in the affirmative supports the argument that the impairment did not impinge on reasonable expectations. Second, did the impairment restrict the parties to their reasonable expectations? Again, an answer in the affirmative supports a finding that there was no impingement on the reasonable expectations. Lastly, did the legislation aim to remedy a problem that was foreseeable at the time of the contract? If the problem was not foreseeable, it supports the idea that reasonable expectations were not impinged.

The first factor comports with both precedent and the Framers' intent. This factor adheres to precedent, as it combines the "reasonable" requirements common to both the *Blaisdell* and *U.S. Trust* tests[230] with factors from the *El Paso* decision.[231] Furthermore, this factor is in line with the Framers' original intent, as it attempts to protect the expectations of the parties, thus advancing the goal of stability and sanctity of contracts.[232]

2. The Second Factor

The second factor of the third prong asks if the impairment was aimed at a legitimate purpose. An answer in the affirmative will favor constitutionality, while an answer in the negative will favor invalidity. Because this question naturally may lead a court to evaluate the policies and decisions of the legislature—an undesirable result—two interrelated sub-questions supplement the inquiry. First, did the impairment protect a basic interest of society? An answer in the affirmative swings in favor of constitutionality. Second, did the impairment advantage particular individuals? Again, an answer in the negative will clearly support the validity of the legislation. These guiding questions will prevent the lower courts from engaging in any kind of deference discussion.

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[230] *See U.S. Trust*, 431 U.S. at 29 ("We can only sustain the repeal of the 1962 covenant if that impairment was both reasonable and necessary to serve the admittedly important purposes claimed by the State."); *Blaisdell*, 290 U.S. at 438 ("The question is . . . whether the legislation is addressed to a legitimate end and the measures taken are reasonable and appropriate to that end.").

[231] City of El Paso v. Simmons, 379 U.S. 497, 515 (1965) ("Laws which restrict a party to those gains reasonably to be expected from the contract are not subject to attack under the Contract Clause, notwithstanding that they technically alter an obligation of a contract.").

[232] *See, e.g.*, Ely Jr., *supra* note 4, at 393.

This second factor is straight from precedent and advances the goals of the Framers.[233] The factor and its sub-questions are derived from *Blaisdell* and have been employed by other courts, including the *U.S. Trust* Court.[234] The second sub-question addresses a goal similar to the Framers' initial purpose of preventing states from passing legislation that freed debtors from their liens—thus advantaging a particular group of individuals.[235] This factor also addresses the *U.S. Trust* Court's concern of legislative self-dealing,[236] as the test will require that "target" to be a broad societal interest.

3. The Third Factor

The third factor will ask if the legislature considered other policy alternatives before choosing to impair the contract. This factor is a less severe version of *U.S. Trust*'s "necessity" requirement. To prevent the court from becoming a super-legislature, this factor only requires a state to show that it reasonably considered other alternatives. The court will not weigh whether these alternatives were less drastic or more appropriate and will accept the alternatives if reasonably considered. The availability of legislative history, minutes, and other reports will mitigate the concern that this factor defers to the state, as the challenger and the court will be able to determine from these records if the state really did consider the alternative offered. Obviously, an affirmative response to this factor supports the constitutionality of the act.

4. The Fourth and Fifth Factors

The fourth and fifth factors are closely related. The fourth factor comes directly from *Blaisdell*, and asks if the state aimed the legislation impairing the contract at an emergency or crisis.[237] Clearly, an answer in the affirmative supports the constitutionality of the measure. The fifth factor also comes from that same *Blaisdell* list of criteria and asks if the legislation is temporary. Again, an answer in the affirmative supports constitutionality.

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[233] *See Blaisdell*, 290 U.S. at 438.
[234] *See id.*; *see, e.g.*, *U.S. Trust*, 431 U.S. at 29.
[235] *See* Ely Jr., *supra* note 4, at 372.
[236] *See U.S. Trust*, 431 U.S. at 26.
[237] *See Blaisdell*, 290 U.S. at 444–45.

These two factors are simple, but integral to the balance of the test. These factors will allow essential legislation to stand. If legislation truly aims at a crucial end—an emergency or crisis—it will be temporary to some extent. The legislation will therefore have the support of two factors, and a court will only need the support of one of the other three to uphold the action. Conversely, legislation that is not aimed at an emergency and is not temporary will have two strikes against it and must survive the other three factors to be constitutional.[238] This result restores the original meaning to the Contracts Clause but with a new flexibility. The Clause will have enough muscle to invalidate legislation, but will not strangle the legislature's ability to respond to emergencies.

B. Application of the New Test

The purpose of the new test is to remedy the ambiguity of the *U.S. Trust* test, better reconcile it with precedent and the Framers' intent, and yet still capture the essence of the *U.S. Trust* test. To show that this test achieves these three objectives, it is necessary to illustrate its application. The test will be applied to two fact patterns the courts have previously encountered: the facts before the Supreme Court in *U.S. Trust* and the facts encountered by the Fourth Circuit in *Baltimore Teachers Union v. Mayor of Baltimore*.[239] The *U.S. Trust* facts will produce the same result that the *U.S. Trust* Court reached, but with more clarity and support for its standard. More importantly, this example will show that the new test is meant to clarify *U.S. Trust* and make it more consistent, not overrule or condemn the opinion. The test's review of the facts in *Baltimore Teachers* will produce a result contrary to the Fourth Circuit's decision. This application shows how the proposed test will prevent courts from warping *U.S. Trust*'s standard to produce an inconsistent or unique result.

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[238] The two factors are not conditional on one another. There can be an emergency without a temporary act, and vice versa. Also, the absence of one of the two is by no means controlling on the outcome of the test.

[239] 6 F.3d 1012 (4th Cir. 1993).

1. *Baltimore Teachers* Under the New Test

The *Baltimore Teachers* court dealt with a budget plan that cut the salaries of various public employees.[240] The appellants were public employees who had previously negotiated their salaries with the City of Baltimore.[241] After Baltimore lost significant state aid, the appellee, City Council of Baltimore, responded with budget cuts.[242] Under this plan, the appellants lost two and a half days of pay and alleged an impairment of their previously negotiated salaries.[243]

a. The First Prong

The first prong asks if there was a substantial impairment of contractual obligations. This question is answered in the affirmative. The budget plan enacted by the appellees cut the appellants' salary by nearly one percent.[244] There was no provision in the contract allowing unilateral alterations to the negotiated salary terms, thus the reduction was an impairment.[245] With the threshold question answered in the affirmative, the analysis moves to the second prong.

b. The Second Prong

The second prong is a reserved powers analysis and asks if the State implicated its reserved powers. The act here does not fall into the eminent domain power or police power, as it addressed a purely financial objective: cutting salaries to save money.[246] Thus, the State's reserved powers are not implicated and the third prong will be evaluated objectively.

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[240] *Id.* at 1014.

[241] *Id.* The appellants, police officers and teachers, would negotiate compensation with the City Council, who then would enact the terms into law for that particular year. *Id.*

[242] *Id.*

[243] *Id.*

[244] *Id.*

[245] *Id.* at 1015–16.

[246] Although it seems strange to discuss the State's reserved powers when a city in the State has acted, no court has addressed this oddity. Both the Fourth Circuit and the Second Circuit made no distinction in the Clause's application when the action challenged was an act of a city, not the State. *See generally id.*

c. The Third Prong: Factor One

The first factor of the third prong asks if the impairment impinged on the reasonable expectations of the parties. Three sub-inquiries guide this question. First, did the legislation prevent the party from obtaining a windfall? This question is answered in the negative, as the legislation cut the salary that the appellants' had bargained for. Second, did the impairment restrict the party to its reasonable expectations? This question is also answered in the negative. The appellants' expectation that the appellees would pay the salary stated in the contract was reasonable because both parties negotiated and agreed to the contract. The legislation impinged on these expectations, it did not enforce them. Third, did the legislation aim to remedy a problem that was foreseeable at the time of the contract? The answer here is less clear, as the appellees could argue that they could not have expected funding cuts when the salaries were negotiated. This may produce an answer in the affirmative, but it is moot since the other two factors of this prong discussed below support the unconstitutionality of the act. Thus, even an answer in the affirmative would result in this factor supporting the unconstitutionality of the act.

d. The Third Prong: Factor Two

The second factor asks if the impairment was aimed at a legitimate purpose. Two sub-questions guide the analysis. First, did the impairment protect a basic interest of society? The answer to this is likely yes, as the cuts were an attempt to generate funds to replace the aid that the State had cut. The appellees can argue that they needed to replace this aid because it funded various basic interests of society. If the appellees can offer any examples, the answer to this question will be yes. Second, did the impairment advantage particular individuals? The answer here is no, as the cuts attempted to raise money that would be spent on the city as a whole. The second factor would thus support the constitutionality of the act.

e. The Third Prong: Factor Three

The third factor asks if the legislature considered other policy alternatives before choosing the impairment. The appellees only need to offer other alternatives they considered to satisfy this prong. The appellees could argue that they first

attempted to balance the budget through layoffs, early retirements, and job abolishments.[247] The appellees could also offer their plan to balance the budget in other ways, such as reallocating other funds and drawing proceeds from property sales.[248] The appellants could argue that the above actions were not alternatives because they were part of the same budget-cut plan and thus were acts in addition to the cuts. Since the impairment involves balancing a budget, the appellees likely would be able to offer alternatives they considered. Thus, the third factor supports the constitutionality of the act.

f. The Third Prong: Factor Four and Factor Five

The fourth factor asks if the act was aimed at an emergency. Although debatable, the answer would likely be no. The appellees could argue that they are required to balance the budget by law, and thus the deficit they faced was a "fiscal crisis."[249] The appellants could argue that the deficit was not an emergency, but instead a regular hardship inherent in running a city. States and cities routinely balance their budgets and deal with deficits and surpluses. Thus, this was not an emergency, it was just another choice the city had to make. The court would likely agree, as balancing a budget is part of a city's everyday duties and it should not be able to repudiate contracts to climb out of debt. Thus, this factor supports the unconstitutionality of the act.

The fifth factor asks if the legislation was temporary. There is no evidence that the appellees intended to reimburse the appellants for their losses, as this would defeat the purpose of the cuts. The appellees could contend that since they stopped the cuts before the fiscal year end, they were only temporary.[250] The appellants could argue that the act was only cut short because the City Council acquired the funds it needed to balance the budget. Finding the impairment temporary would allow the city to cut salaries whenever they needed to balance the budget. This argument best captures the fifth factor's purpose and will support the unconstitutionality of the act.

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[247] *Id.* at 1020.
[248] *Id.* at 1020 n.12.
[249] *Id.* at 1020.
[250] *Id.*

g. Conclusion

The proposed test would result in the invalidation of the State's action. Three of the five factors supported the unconstitutionality of the act, while only two supported the constitutionality. This application emphasizes how the proposed test prevents courts from exploiting the ambiguity of *U.S. Trust* to achieve their desired result. In actuality, the Fourth Circuit upheld the legislation because it was reluctant to sit as a super-legislature and evaluate the appropriateness of the cuts.[251] This example exhibits how the proposed test removes the discretion and subjectivity from the court's approach and installs a clear, systematic approach.

2. *U.S. Trust* Under the New Test

The *U.S. Trust* Court dealt with the repeal of a covenant between the State of New Jersey and bondholders.[252] The covenant dealt with the railroad expansion project of the Port Authority of New Jersey and stated that as long as bonds funding the project remained unpaid, the State could not fund any improvements to the railroad using the revenues and reserves of Port Authority's mass transit system.[253] In 1972, the Port Authority wished to expand the mass transit system.[254] When federal funding for the project fell through, New Jersey repealed the covenant and raised tolls to fund the expansion project.[255] The appellant alleged a violation of the Contracts Clause.[256]

a. The First Prong

Under the proposed test, the first prong would ask whether there was a substantial impairment of contractual obligations. The answer here is clearly yes, as the repeal eliminated an important security provision that the appellant had bargained for.[257] With the threshold question satisfied, the court would then move to the second question.

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[251] *Id.* at 1021–22.

[252] *See* U.S. Trust Co. v. New Jersey, 431 U.S. 1, 20–21 (1977).

[253] *Id.* at 10. This Note refrains from delving into the vast complexity of the covenant and for the sake of simplicity, has only presented the facts necessary for understanding the application of the test.

[254] *See id.* at 12–13.

[255] *See id.* at 13–14.

[256] *See id.* at 17.

[257] *See id.* at 19.

b. The Second Prong

The second question is the reserved powers analysis, which asks if the State contracted away a reserved power. If the State contracted away its eminent domain power or police power, the contract will be considered invalid and thus no impairment could have occurred. If one of these powers is not implicated, the State's justifications will be evaluated objectively. Here, the State argued that it repealed the covenant pursuant to New Jersey's police power, as it aimed at serving the public interest, namely mass transportation and energy conservation.[258] The court would likely classify the repeal outside of the reserved powers.[259] This is because the repeal was purely financially driven: New Jersey needed more money to invest into the Port Authority, and it thus repealed a limitation on its finances. Since the State did not contract away a reserved power, the court will review the State's justifications objectively.

c. The Third Prong: Factor One

The first factor asks if the impairment impinged on the reasonable expectations of the party. Three sub-inquiries help to answer this question. First, the court will ask if the legislation prevented the party from obtaining a windfall. This is not the case here, as the legislation repealed a security provision that protected the funds needed to repay the bondholders. The answer in the negative here supports the unconstitutionality of the repeal. The second sub-inquiry asks if the impairment restricted the parties to their reasonable expectations. Again, the repeal eliminated an important, bargained-for security provision. The State destroyed the parties' reasonable expectations when it repealed the covenant, as the appellant lost the security provision that guaranteed repayment. This answer in the negative supports the unconstitutionality of the repeal.

The third sub-inquiry asks if the legislation aimed to remedy a problem that was unforeseeable at the time of the contract. Again, the answer here is likely no. Mass transit had been a rising public concern since the early twentieth century,[260] and it is unlikely the State would not have expected a need to expand.

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[258] *Id.* at 28–29.
[259] *Id.* at 23–25.
[260] *See id.* at 31–32.

The State could argue that it could not have expected the demand for expansion to be so high. Although this may be a valid argument, the answer is moot since the first and second sub-inquiries will support the unconstitutionality of the repeal. Therefore, the first factor supports the unconstitutionality of the impairment.

d. The Third Prong: Factor Two

The second factor asks if the impairment was aimed at a legitimate public purpose. The first guiding sub-inquiry asks if the impairment protected a basic interest of society. The contract was impaired due to a repeal that enabled the expansion of mass transit. Mass transit is a basic interest of society in itself. It also implicates energy conservation and environmental protection. An increase in the use of mass transit would likely result in a decrease of automobile use. This decrease will lead to less petroleum consumption, benefiting both the environment and the conservation of energy, thus protecting those two basic interests of society.

The second sub-inquiry asks if the impairment advantaged particular individuals. This question is answered in the negative, since the expansion of mass transit, the protection of the environment, and the conservation of energy benefits society, not specific individuals. Both sub-inquiries support upholding the act, thus the second factor supports the constitutionality of the repeal.

e. The Third Prong: Factor Three

The third factor asks if the legislature considered other policy alternatives before resorting to the action that impaired the contract. Here, the State could argue it did consider other alternatives when it attempted to raise the money for expansion from federal aid.[261] The appellant could argue that this is irrelevant because the State passed the repeal in *response* to the withdrawal of federal funding, not as an alternative to federal funding. If the State was able to offer a reasonable example of an alternative it considered, the court could review the legislative records to determine if the State actually did consider that alternative. Here, the low hurdle for the State makes it likely

[261] *Id.* at 12–13.

that the factor will support the constitutionality. The point is moot, however, since the remaining factors support the unconstitutionality of the repeal.

f. The Third Prong: Factors Four and Five

The fourth and fifth factors often go hand-in-hand and courts will often analyze them together. The fourth factor asks if the impairment aimed to remedy an emergency or crisis. This question is answered in the negative, as the need for money to expand mass transit is not an emergency. The State could argue here that there was a declared national petroleum shortage,[262] and the impairment remedied this petroleum shortage by attempting to decrease automobile use. The court could look to legislative history to determine if an emergency actually spurred the repeal. Since the repeal was more likely to raise money for the expansion plan because federal grants fell through, it likely was not a response to an emergency and therefore supports the unconstitutionality.[263]

The fifth factor asks if the legislation or impairment was temporary. This question is also answered in the negative. The State repealed its original covenant with the appellant and installed no mechanism that would reinstate the original covenant after a certain amount of time.[264] Moreover, there was no guarantee that the Port Authority would stop using the revenue to subsidize the improvements once the initial expansion was complete. The fifth factor thus would support the unconstitutionality of the impairment.

g. Conclusion

The application of the proposed test to the *U.S. Trust* scenario would have resulted in three factors supporting the unconstitutionality of the impairment and two factors supporting the constitutionality.[265] The result aligns with the actual result

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[262] *See id.* at 13–14.

[263] Before the federal grants fell through, the State actually had adequate funding to go forward. *See id.* at 13.

[264] *See id.* at 14 (discussing the repeal with no mention of reinstatement of the original covenant).

[265] The author assumes the State would be able to offer evidence that it considered other alternatives to pass the third factor. The first, fourth, and fifth factors support unconstitutionality, while the second and third factors support constitutionality.

of *U.S. Trust*. This result illustrates how the proposed test attempts to capture the essence of *U.S. Trust*, but with modifications, to remedy the ambiguities and inconsistencies that rendered it unworkable.

CONCLUSION

The new test for a Contracts Clause violation seeks to draw on the principles of Contracts Clause jurisprudence and the original intent of the Framers and seeks to improve a doctrine that has been misinterpreted and misapplied over the years. The proposed test does not take the "modern" approach of affording high protection to public contracts but also does not return the Clause back to the useless tool it was before *U.S. Trust*. Both *Blaisdell* and *U.S. Trust* had strengths and weaknesses, thus evidencing why the middle ground between the two is the best approach. This test seeks to return the Contracts Clause's power while still allowing state legislatures to retain their essential attributes of sovereignty and ability to respond to pressing public needs.