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Trail Mountain Coal Co. v. Utah Division of State Lands & Forestry: Can States Retroactively Alter Their Own Contractual Obligations?

I. INTRODUCTION

Article I, Section 10 of the United States Constitution (the Contract Clause) prohibits the States from passing any "Law impairing the Obligation of Contracts." Like most other constitutional protections, the limits of the Contract Clause are often difficult to define. In a recent decision, *Trail Mountain Coal Co. v. Utah Division of State Lands & Forestry*,[1] the Utah Supreme Court declined to apply Contract Clause scrutiny to Utah's default prejudgment interest rate statute.[2] In so doing, the court dismissed over 150 years of Contract Clause jurisprudence and opened the constitutional door for states to alter their own contractual obligations by retroactively changing the law.

This Note discusses the background, reasoning, and implications of the *Trail Mountain* decision. Section II provides a brief overview of the United States Supreme Court's Contract Clause jurisprudence. Section III outlines the factual background of the *Trail Mountain* dispute. Section IV summarizes the court's decision in the case. Section V evaluates the court's reasoning, arguing that the *Trail Mountain* decision was based upon an incorrect interpretation of the Contract Clause. This Note concludes that the Utah Supreme Court's decision could dramatically loosen the restrictions of the Contract Clause, thereby permitting states to modify their own contractual obligations so long as they can articulate a justification based upon state law.

II. BACKGROUND

Throughout the 1800s, the Contract Clause—as a portion of Article I, Section 10 has come to be known—was generally con-

1. 921 P.2d 1365 (Utah 1996), *cert. denied*, 117 S. Ct. 1017 (1997).

2. *See id.* at 1367-69. Utah's default prejudgment interest rate statute is found in UTAH CODE ANN. § 15-1-1(2) (1953).

sidered "the major [constitutional] restraint on state economic regulation."[3] In fact, legal historians note that during the early years of our nation's history, "the Contract Clause was the constitutional rule most frequently invoked to strike down state legislation."[4]

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3. GERALD GUNTHER, CONSTITUTIONAL LAW 478 (12th ed. 1991) (charting the dramatic evolution of the Supreme Court's interpretation of the Contract Clause).

The Court's early Contract Clause cases provided extensive protection to contractual rights. In *Fletcher v. Peck*, 10 U.S. (6 Cranch) 87 (1810), the Court held that the Contract Clause prohibited the State of Georgia from declaring void a fraudulently obtained land title (which the original grantee had acquired from the State by bribing state legislators) where that title was subsequently conveyed to a good-faith purchaser. Chief Justice Marshall explained:

> [I]n this case, the estate having passed into tha hands of a purchaser for a valuable consideration, without notice, the state of Georgia was restrained, either by general principles which are common to our free institutions, or by the particular provisions of tha Constitution of the United States, from passing a law whereby the estate of the plaintiff in the premises so purchased could be constitutionally and legally impaired and rendered null and void.

Id. at 139. In other words, the Court held that even where a State enters into a contract (the Court treated the grant as an "executed contract") under illegal or quasi-legal circumstances, it cannot subsequently repudiate that contract.

In *Sturges v. Crowninshield*, 17 U.S. (4 Wheat.) 122 (1819), the Court demonstrated its willingness to strike down legislation interfering with private contracts, invalidating a New York debtor relief law under which debtors could be forgiven if they would agree to forfeit their property. In another case, Chief Justice Marshall explained that New York's law created the kind of interference that provided the Framers with the "great motive for imposing this restriction on the State legislatures." Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 644 (1819). *But see* Ogden v. Saunders, 25 U.S. (12 Wheat.) 213 (1827) (upholding nonretroactive application of a similar law).

This early, broad-sweeping interpretation set the stage for over a century of liberal Contract Clause interpretation. *See* Robert A. Graham, *The Constitution, the Legislature, and Unfair Surprise: Toward a Reliance-Based Approach to the Contract Clause*, 92 MICH. L. REV. 398 (1997).

4. Graham, *supra* note 3, at 398. However, this is not to say that because the Court rendered broad interpretations of the Contract Clause, it uniformly invoked the heavy hand of constitutional scrutiny every time a State action arguably interfered with a contract. The Court's Contract Clause appeared to have at least some limits. For example, the Court declined to invalidata state interference with a public grant in *Dartmouth College v. Woodward*, 17 U.S. (4 Wheat.) 518 (1819). Chief Justice Marshall explained:

> It is more than possible that the preservation of rights of this description was not particularly in tha view of the framers of the constitution. . . . It is probable, that interferences of more frequent occurrence . . . [where] the mischief was more extensive, constituted the great motive for imposing this restriction on the state legislatures.

Id. at 644.

By the same token, the Court did not always view state action obliterating contracts in the same light as state action altering the remedies available for a contractual breach. *See* LAWRENCE H. TRIBE, AMERICAN CONSTITUTIONAL LAW § 9-9, at

The "glory days" of the Contract Clause came to a screeching halt in the 1930s with the Court's decision in *Home Building & Loan Ass'n v. Blaisdell*.[5] In that case, the Court rejected a Contract Clause challenge to a Minnesota statute that extended the period of time that a mortgage holder could be in default before the lender could force a foreclosure sale.[6] The Court based its conclusion on the argument that the state was justified in interfering with contractual obligations when an economic emergency demanded that the State enact such a statute in order to protect a community's general welfare. The Court concluded that the economic emergency that existed at the time the statute was passed—the Great Depression—"furnished a proper occasion for the exercise of the reserved power of the State to protect the vital interests of the community."[7] Since earlier cases had been driven by a nondeferential analysis, *Blaisdell* constituted a dramatic departure from the Court's previously onerous Contract Clause scrutiny, opening the constitutional door for more economically restrictive state regulations.[8]

In 1977, the Court's Contract Clause jurisprudence reached an important turning point in *United States Trust Co. v. New Jersey*[9] when, for the first time in almost forty years, the Court invalidated a state law under the Contract Clause. The dispute in *United States Trust* arose when New Jersey rescinded its statutory covenant not to subsidize (through the Port Authority of New York and New Jersey) rail passenger transportation with

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615 (2d ed. 1988) ("From the beginning, the Court had announced a distinction between laws impairing a contract's *obligation* and those merely modifying the *remedies* provided for its enforcement." (citing Sturges v. Crownwinshield, 17 U.S. (4 Wheat.) 122, 199-207 (1819))).

5. 290 U.S. 398 (1934).

6. *See id.* at 415-18.

7. *Id.* at 444-47.

8. After *Blaisdell*, states were given more regulatory latitude under the Contract Clause. *See, e.g.*, El Paso v. Simmons, 379 U.S. 497 (1965) (upholding a Texas law shortening the time period during which certain landowners could reestablish their ownership by paying back taxes); *see also* Sherry Young, *Is "Due Process" Unconstitutional? The NCAA Wins Round One In Its Fight Against Regulation of its Enforcement Proceedings*, 25 ARIZ. ST. L.J. 841, 877 (1993) ("*Blaisdell* was a watershed case in Contract Clause jurisprudence. *Blaisdell* established the proposition that the near absolute prohibition on the impairment of contracts is subordinate to the state's power to legislate in the public interest. *Blaisdell* also marked the beginning of an era of extremely deferential review of state legislation challenged on Contract Clause grounds.").

9. 431 U.S. 1 (1977).

bond revenues and reserves.[10] Bondholders brought suit, claiming that the rescission constituted a violation of the Contract Clause since, in purchasing Port Authority bonds, they had relied on the State's covenant not to use bond money to subsidize traditionally unprofitable endeavors like railway passenger transportation.[11]

In *United States Trust*, the Court held that laws impairing a state's own contractual obligations are entitled to less deference under the Contract Clause than are laws that merely affect private contracts to which the state is not a party.[12] Writing for the Court, Justice Blackmun explained that such laws are constitutional only when they are "reasonable and necessary to serve an important public purpose,"[13] and that New Jersey's action here was "neither necessary to achievement of the [comprehensive transportation] plan nor reasonable in light of the circumstances."[14] He also rejected the argument that the Contract Clause is implicated only where the State's action has created a "total destruction" of contractual obligations.[15]

One year later, in *Allied Structural Steel Co. v. Spannaus*,[16] the Court declared unconstitutional Minnesota's Private Pension Benefits Protection Act—which required private employers with pension plans to pay a penalty if their pension plans could not cover the pensions of all employees who had worked for the employer for more than ten years—as applied to employers whose already-existing employment contracts provided pension plans but did not provide for all employees who had worked at least ten years.[17] *Allied Structural Steel* was significant in that it ap-

10. *See id.* at 4-5.

11. *See id.* at 25.

12. *See id.* at 25-26.

13. *Id.* Justice Blackmun pointed out that when state action interferes with private contractual obligations "courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure" because this standard is "customary in reviewing economic and social regulation." *Id.* at 22-23.

He added that the reason for the "dual standard" inherent in Contract Clause analysis resulted from the fear that 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." *Id.* at 26.

14. *Id.* at 29. He reached this conclusion because New Jersey's action constituted a "drastic impairment" and a "more moderate course would serve its purposes equally well." *Id.* at 31.

15. *See id.* at 26-27.

16. 438 U.S. 234 (1978).

17. *See id.* at 236-40, 250.

peared to apply *United States Trust's* nondeferential Contract Clause scrutiny to private contracts, and seemed to shift the emphasis of the Court's inquiry from whether the state was a party to the allegedly impaired contract to whether the severity of the contractual impairment was significant enough to implicate the Contract Clause.[18] Writing for the Court, Justice Stewart explained:

> [The] severity of the impairment measures the height of the hurdle the state legislation must clear. Minimal alteration of contractual obligations may end the inquiry at its first stage. Severe impairment, on the other hand, will push the inquiry to a careful examination of the nature and purpose of the state legislation.
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> . . . .
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> . . . [In the case at bar, the steel company] had no reason to anticipate that its employees' pension rights could become vested except in accordance with the terms of the plan. It relied heavily, and reasonably, on this legitimate contractual expectation in calculating its annual contributions to the pension fund.[19]

In other words, where reliance on a preexisting contract is reasonable and where such reliance proves detrimental when the state interferes, the state's action will be considered "severe." Likewise, the deferential nature of the Court's Contract Clause scrutiny is inversely proportional to the severity of the challenged law's contractual interference.[20]

In 1983, the Court combined the public/private contract distinction test from *United States Trust* and the "severity" test from *Allied Structural Steel*. In *Energy Reserves Group v. Kansas Power & Light Co.*,[21] the Court upheld a Kansas law that indirectly altered the pricing scheme between a natural gas company and an electric utility company. In a unanimous opinion, Justice Blackmun outlined a three-pronged test for determining whether a state action violated the Contract Clause.[22]

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18. *See id.* at 244-45.
19. *Id.* at 245-46.
20. *See id.*
21. 459 U.S. 400 (1983).
22. Justice Blackmun's list constituted an amalgamation of the Court's previous holdings in this area. *See id.* at 411-13.

First, the Court would consider "'whether the state law has, in fact, operated as a substantial impairment of a contractual relationship.'"[23] Second, "[i]f the state regulation constitutes a substantial impairment, the State, in justification, must have a significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem."[24] Third, "[o]nce a legitimate public purpose has been identified," the Court must decide

> whether 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." Unless the State itself is a contracting party, "[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."[25]

In other words, state alterations of contracts to which the state is a party will be reviewed strictly, while similar alterations of private contracts will be given substantial deference under the Contract Clause.

In the same term, the Court rejected another Contract Clause challenge in *Exxon Corp. v. Eagerton*,[26] when it upheld an Alabama law that forbade oil and gas producers from passing the costs of new taxes on to consumers. The challengers claimed that the law eviscerated key provisions of existing contracts that specifically allowed them to pass such costs to the consumer.

Writing for a unanimous Court, Justice Marshall explained that the three-part test laid out in *Energy Reserves* was inapposite here because the law challenged was "generally applicable" and not directly aimed at altering contracts.[27] The Court noted

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23. *Id.* at 411 (quoting *Allied Structural Steel*, 438 U.S. at 244). Blackmun added that

> [t]he severity of the impairment is said to increase the level of [the inquiry]. Total destruction of contractual expectations is not necessary for a finding of substantial impairment. . . . [To] determin[e] the extent of the impairment, we are to consider whether the industry the complaining party has entered has been regulated in the past.

Id. (citations omitted).

24. *Id.* at 411-12 (citing *Allied Structural Steel*, 438 U.S. at 247, 249; United States Trust Co. v. New Jersey, 431 U.S. 1, 22 (1977)).

25. *Id.* (quoting *United States Trust*, 431 U.S. at 22-23).

26. 462 U.S. 176 (1983).

27. *Id.* at 191. Marshall elaborated, arguing that "[l]ike the laws upheld in [this

that the outcome may have differed had the State been a party to the contract because of "special concerns associated with a State's impairment of it own contractual obligations."[28]

In 1992, the Court revisited the Contract Clause question in *General Motors Corp. v. Romein*,[29] when General Motors challenged a Michigan law that altered the workers' compensation requirements. General Motors claimed that the law violated the Contract Clause because the company had relied on earlier, less exacting workers' compensation laws when drafting preexisting employment contracts. General Motors' claim centered around the assertion that the earlier laws were somehow "incorporated" into their employees' contracts.[30] In analyzing the case, the Court began with the first inquiry in the three-part test outlined in *Kansas Power & Light*, pointing out that "[g]enerally, we first ask whether the change in state law has 'operated a substantial impairment of a contractual relationship.'"[31] The Court explained that "[t]his [first] inquiry has three components: [1] whether there is a contractual relationship, [2] whether a change in law impairs that contractual relationship, and [3] whether the impairment is substantial."[32]

The Court flatly rejected the challenge, holding that no contract existed.[33] While noting that, in many instances, laws in

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Court's previous] cases, the [law challenged here] did not prescribe a rule limited in effect to contractual obligations or remedies, but instead imposed a generally applicable rule of conduct designed to advance 'a broad societal interest' . . . . [Therefore, the law] is sharply distinguishable from the measures struck down in [*United States Trust* and *Allied Structural Steel*]" since the laws stricken in both of those cases had the "sole effect" of changing contractual obligations. *Id.* at 191-92 (citations omitted) (quoting *Allied Structural Steel*, 438 U.S. at 249).

28. *Id.* at 192 n.13. The Eighth Circuit recently discussed this principle, explaining that "[a]lthough states have broad discretion under their police powers to regulate existing contractual relationships, such regulation must protect a 'broad societal interest rather than a narrow class.'" *In re* Workers' Compensation Refund, 46 F.3d 813, 820 (8th Cir. 1995) (quoting *Allied Structural Steel*, 438 U.S. at 249).

29. 503 U.S. 181 (1992).

30. *See id.* at 188.

31. *Id.* at 186 (quoting *Allied Structural Steel*, 438 U.S. at 244); *accord* Energy Reserves Group, Inc. v. Kansas Power & Light Co., 459 U.S. 400, 411 (1983)); *supra* text accompanying notes 23-25.

32. *Romein*, 503 U.S. at 186.

33. *See id.* at 186-87 (explaining that "[n]ormally, the first two are unproblematic, and we need address only the third. In this case, however, we need not reach the questions of impairment, as we hold that there was no contractual agreement regarding the specific workers' compensation terms allegedly at issue.").

General Motors had argued:

[T]he workers' compensation law is an implied term of the contracts, because

existence at the time of assent are considered contractual terms for Commerce Clause purposes,[34] the Court found that the laws in place at the time General Motors signed the contracts were not incorporated into the contracts for Contract Clause purposes because later amendment of those laws did not alter the parties' "ability to enforce the bargained-for terms of the employment contracts."[35] In other words, when a State passes a law amending or eviscerating an earlier law upon which parties to a contract had relied, the new law may not violate the Contract Clause if it does not "affect the validity, construction, and enforcement" of the contract in question.[36]

> the parties bargained for other compensation with workers' compensation benefits in mind. This implied term that was allegedly impaired by the [law in question] is defined as a promise to pay the amount of workers' compensation required by law for each payment period.

Id. at 187. General Motors further asserted that "[o]nce performance of this obligation is completed by making payments for any disability period," they had "a settled expectation that [could not] be undone by later state legislation." *Id.*

34. The Court reached this conclusion noting that if the facts had been slightly different, General Motors might have had a valid claim:

> While it is somewhat misleading to characterize laws affecting the enforceability of contracts as "incorporated terms" of a contract, these laws are subject to Contract Clause analysis because without them, contracts are reduced to simple, unenforceable promises. . . . A change in the remedies available under a contract, for example, may convert an agreement enforceable at law into a mere promise, thereby impairing the contract's obligatory force. For this reason, changes in the laws that make a contract legally enforceable may trigger Contract Clause scrutiny if they impair the obligation of pre-existing contracts, even if they do not alter any of the contracts' bargained-for terms.

Id. at 189 (citations omitted).

35. *Id.* at 190.

36. *Id.* at 189 (citing United States Trust Co. v. New Jersey, 431 U.S. 1, 19 n.17 (1977)). The Court concluded by observing that this holding was necessary because a broader holding would demand that courts

> should read every workplace regulation into the private contractual arrangements of employers and employees [and] would expand the definition of contract so far that the constitutional provision would lose its anchoring purpose, *i.e.*, "enabl[ing] individuals to order their personal and business affairs according to their particular needs and interests." Instead, the Clause would protect against all changes . . . on bargained-for agreements. The employment contract, in [G.M.'s] view, could incorporate workplace safety regulations, employment tax obligations, and laws prohibiting workplace discrimination, even if these laws are not intended to affect private contracts and are not subject to bargaining between the employer and employees. Moreover, [G.M.'s] construction would severely limit the ability of state legislatures to amend their regulatory legislation. Amendments could not take effect until all existing contracts expired, and parties could evade regulation by entering into long-term contracts.

The Court's current Contract Clause jurisprudence can be summarized in one paragraph. While the three-part test from *Kansas Power & Light*[37] is still good law, the Court currently applies a sort of heightened Contract Clause scrutiny to state actions that alter a state's own contractual obligations, while giving deferential treatment to state actions that affect only private contracts.[38] In addition, the Court may find that a state has violated the Contract Clause even when the state has not "alter[ed] any of the contracts' bargained-for terms"[39] if the state's retroactive change in law "affect[s] the validity, construction, and enforcement of contracts."[40]

III. THE *TRAIL MOUNTAIN* DISPUTE

In 1965, Trail Mountain Coal Company's predecessors-in-interest entered into a coal lease agreement with the State of Utah allowing them to extract coal from a plot of land owned by the State.[41] Under the terms of the agreement, the lessee was required to pay the state royalties for all coal mined on the property. The royalties were to be determined under one of two possible rates: the lessee would pay the higher of either (1) fifteen cents per ton of coal extracted from the mine or (2) "the rate

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Id. at 190 (quoting *Allied Structural Steel*, 438 U.S. at 245).

37. *See* Energy Reserves Group Inc. v. Kansas Power & Light Co., 459 U.S. 400, 411-13 (1983) (outlining the three components of the test: (1) "whether the state law has, in fact, operated as a substantial impairment," (2) "the State, in justification, must have a significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem," and (3) "[o]nce a legitimate purpose has been identified," the Court must decide "whether the adjustment of 'the rights and responsibilities of contracting parties' [results from the challenged law]. Unless the State itself is a contracting party, '[a]s is customary in reviewing economic and social legislation, . . . courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure.'" (alteration in original) (citations omitted) (quoting United States Trust Co. v. New Jersey, 431 U.S. 1, 22-23 (1977))).

38. The Court has explained that it will sustain legislation thet (1) is "generally applicable" and not aimed at precise contractual obligations, Exxon Corp. v. Eagerton, 462 U.S. 176, 191 (1983), or (2) merely changes earlier legislation that was not "incorporated" into a contract, *Romein*, 503 U.S. at 189-90, and did not affect that contract's "validity, construction, and enforce[ability]," *United States Trust*, 431 U.S. at 19 n.1.

39. *Romein*, 503 U.S. at 189.

40. *Id.* (citing *United States Trust*, 431 U.S. at 19 n.17).

41. *See* Trail Mountain Coal Co. v. Utah Div. of State Lands & Forestry, 921 P.2d 1365, 1367 (Utah 1996).

prevailing . . . for federal leases of land of similar character under coal leases issued by the United States at that time."[42]

The lease agreement itself contained no express language providing for a prejudgment interest rate arising from a possible breach of contract. However, a Utah statute filled in the gap, providing that "[u]nless the parties to a lawful contract specify a different rate of interest, the legal rate of interest for the loan or forbearance of any money, goods, or chose in action shall be 6% per annum."[43] Thus, by declining to include a prejudgment interest provision, the parties to the Agreement implicitly agreed that if either party breached the terms of the contract, that party would pay six percent of the value (annually) of the contractual breach.

The first royalty rate (under which lessee paid fifteen cents per ton) remained in effect for the first eleven years of the lease.[44] In 1976, Congress passed the Federal Coal Leasing Amendments Act,[45] calling for new regulations that ultimately required holders of federal coal leases to pay a royalty "not less than 8 percent of the value of the coal removed."[46]

When "'8 percent of the value of the coal removed'"[47] became the royalty rate for federal coal leases, it appeared that Trail Mountain's predecessors would have to pay that eight percent since it required the lessee to pay more than the fifteen cents per ton.[48] However, when Trail Mountain's predecessors inquired about the possible rate change, the Division of State Lands and Forestry apparently informed them that "15 cents per ton was the correct rate for the Lease."[49] The Division apparently decided that the change in federal coal lease royalty rates would not affect state coal lease rates until "Federal leases in the same area [as the lease in question]" were paying the higher rate.[50]

Several years later, the Division conducted financial audits of

42. *Id.*

43. UTAH CODE ANN. § 15-1-1(2) (1953).

44. *See Trail Mountain*, 921 P.2d at 1367.

45. 30 U.S.C. §§ 201-09 (1976).

46. 43 C.F.R. § 3473.3-2(a)(3) (1979).

47. *Trail Mountain*, 921 P.2d at 1367 (quoting 43 C.F.R. § 3473.3-2(a)(3)).

48. *See id.* Under the lease, the lessee was required to pay royalties under one of the two rates outlined in the Agreement, "whichever is higher." *Id.*

49. *Id.* at 1368. As the court noted, the Division continued to accept Trail Mountain's 15¢ per ton royalty payments without protest.

50. Letter from C.J. Brinton, Economic Geographer, to John L. Bell (Oct. 4, 1976) (on file with the *Brigham Young University Law Review*).

several of the state's coal leases. In the course of the audit, the Division repudiated its earlier assurances that the fifteen cents per ton rate still applied, concluding that the higher royalty rate went into effect in 1976 when the federal government began issuing new leases under the eight percent rate (regardless of the location of the new leases).[51] As a result, the Division concluded that Trail Mountain had not paid the full amount of royalties required by the agreement, and that it owed the State $3,351,474.75.[52] Even though the default resulted from Trail Mountain's reliance on the Division's assurances that the royalty rate had not changed, the Division ordered Trail Mountain to pay prejudgment interest on the unpaid royalty sum amounting to $1,854,115.69.[53] In addition, the Division assessed a late payment penalty of $16,606.76.[54]

In calculating the amount of prejudgment interest that Trail Mountain allegedly owed, the Division applied the six percent prejudgment default interest rate (provided by the law that was in operation at the time the Agreement was made)[55] to the default sum that had accrued through June 30, 1981.[56] However, the Division concluded that changes in the law[57] dictated that the interest rate for all debts accrued between July 1, 1981 and November 30, 1982 should be ten percent.[58] The Division further asserted that because the State had adopted a separate regulation regarding royalty payment defaults in November of 1982, the interest rate for all debts accrued between December 1, 1982 and October 15, 1985 should be eighteen percent.[59]

Trail Mountain filed suit in a Utah trial court to enjoin the Division from collecting the back royalties, assessing the late payment penalty, and applying the increased interest rates.[60]

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51. *See Trail Mountain*, 921 P.2d at 1367.
52. *See id.*
53. *See id.*
54. *See id.*
55. *See* UTAH CODE ANN. § 15-1-1(2) (1953).
56. *See Trail Mountain*, 921 P.2d at 1368.
57. *See* UTAH CODE ANN. § 15-1-1 (1982). This statute did not apply "to any contract or obligations made before May 14, 1981." *Id.* Since the Agreement was signed in 1965, this section (by its own terms) did not apply to Trail Mountain's lease.
58. *See Trail Mountain*, 921 P.2d at 1368.
59. *See id.*
60. *See id.*

The trial court held for Trail Mountain on a motion for summary judgment.[61]

The Utah Court of Appeals consolidated the case with three similar actions, reversed the trial court's holding, and remanded all three cases for individual adjudication.[62] The trial court then concluded that while the Division could require Trail Mountain to pay the higher royalty rate for the period in question, interest on the debt that had accrued during the period should be calculated at six percent, as prescribed by the statute in operation at the time the Agreement was signed.[63] Trail Mountain appealed, claiming it was entitled to a deduction for certain transportation costs, and the Division cross-appealed, claiming that the higher interest rates should have applied.[64]

Meanwhile, Consolidation Coal Company, one of the other parties from the consolidated action, appealed from a similar trial court ruling. The Utah Supreme Court accepted that appeal, but transferred Trail Mountain's appeal to the Utah Court of Appeals.[65] The court of appeals explained the trial court's determination on the propriety of applying the six percent royalty was correct.[66] However, the court of appeals reversed the trial court's holding, explaining that Trail Mountain's entire action was barred by the seven-year statute of limitations.[67] The court of appeals also added that even if the action was not time-barred, interest on the late royalty payments would not begin to accrue until after the Division began demanding payment at the eight percent rate.[68]

Less than two months later, the Utah Supreme Court announced its decision in the Consolidation Coal Company's appeal.[69] The supreme court acknowledged the factual and legal similarities between the *Consolidation Coal* case and the *Trail Mountain* case. However, the supreme court's holding in *Consolidation Coal* differed significantly from the court of appeals' *Trail Mountain* decision. In *Consolidation Coal*, the supreme court

61. *See id.*
62. *See id.*
63. *See id.*
64. *See id.*
65. *See id.*
66. *See id.*
67. *See id.; see also* UTAH CODE ANN. § 78-12-2 (1994).
68. *See Trail Mountain*, 921 P.2d at 1368.
69. Consolidation Coal Co. v. Utah Div. of State Lands & Forestry, 886 P.2d 514 (Utah 1994).

held that the Division's prejudgment interest rate determination superseded the original statutory six percent interest rate. The court reasoned that "[t]he State has an irrevocable [constitutional] duty to manage . . . trust lands for the sole benefit of the common schools and to receive 'full value' from any disposition of its school trust lands."[70] In so doing, the supreme court "implicitly rejected *Trail Mountain's* holding that interest payments did not begin to accrue until the Division demanded payment on the back royalties."[71]

On appeal to the Utah Supreme Court in *Trail Mountain*, the Division raised arguments similar to those it had used (successfully) in *Consolidation Coal*. Principally, the Division argued that the court of appeals erred in applying the originally prescribed six percent interest rate to the royalty default debt, and asserted that the Division was justified in imposing the higher interest rate because it had a "constitutional obligation to obtain 'full value' from any disposition of school trust lands."[72]

Among its other assertions,[73] Trail Mountain argued that retroactive application of the Division's prejudgment interest rates violated the Contract Clause of the United States Constitution.[74]

IV. THE UTAH SUPREME COURT'S OPINION

The supreme court quickly dismissed Trail Mountain's Contract Clause claims, reasoning that since the Division had the authority to change the prejudgment interest rate and since the agreement (by its own terms) was "expressly subject to the laws of Utah," the State's action here did not violate the Contract Clause.[75] The court began its analysis by explaining why the State had the authority to retroactively alter the prejudgment

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70. *Id.* at 525 (citing Lassen v. Arizona *ex rel.* Arizona Highway Dep't, 385 U.S. 458, 466 (1967).

71. *Trail Mountain*, 921 P.2d at 1369; *see also Consolidation Coal*, 886 P.2d at 524.

72. *Trail Mountain*, 921 P.2d at 1369.

73. Petitioner Trail Mountain also argued that the Division's actions were improper under the Contract Clause of the Utah Constitution and that the entire action was barred by the statute of limitations. In its holding, the court did not differentiate between the Utah and United States Constitutions, *see id.* at 1369-70, and rejected the statute of limitations argument. *See id.* at 1371.

74. *See id.* at 1369-70.

75. *Id.* at 1369.

interest rate. Citing its own decision in *Consolidation Coal*, the court reiterated its position:

> [T]he specific constitutional requirement that the State obtain full value for its school trust lands, in conjunction with the legislature's broad grant of authority to the Board and our case law indicating that the Board has such further implied powers as are reasonably necessary to carry out its constitutional duties, mandates the conclusion that the Board is empowered to set interest rates and penalties regarding school trust lands.[76]

In other words, the Division clearly had authority under state law to alter the prejudgment interest rates.

The court continued by explaining that the express terms of the agreement itself revealed that all of its provisions were "subject to the laws of Utah."[77] This led the court to conclude that "when the Division sought to enforce the interest and penalty measures promulgated by the Board, it was merely acting pursuant to a right it held under the contract, and no contractual term of the Lease was impaired."[78] Thus, the Utah Supreme Court held that a state may change the terms of a contract to which it is a party without contravening the Contract Clause so long as that contract is subject to the laws of the state.

The court hypothesized that its conclusions may have been different had the prejudgment interest rate been imposed by the words within the four corners of the agreement itself (rather than by a statute in existence at the time of contracting).[79] As the court explained,

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76. *Id.* at 1369 (quoting *Consolidation Coal*, 886 P.2d at 527).

77. *Id.*

78. *Id.* at 1370. The court conceded in a footnote:

> Obviously, there are natural limits to such provisions. The State cannot simply opt out of Contract Clause scrutiny by including such language in all of their contractual agreements and then subsequently rely upon a legislative edict that otherwise clearly violates the Contract Clause. However, in this case we are not dealing with an unanticipated legislative action which abrogates the validity or enforcement of a provision of the contract at issue. Rather, Trail Mountain's Lease specifically provided for regulation by specific agencies, and the regulations that were actually imposed merely prescribed the method of calculating compensation for violation of the terms of the Lease. Hence, the nature and source of the interest and penalty provisions were reasonably foreseeable, and their imposition did not alter any of the essential elements of the contract.

Id. at 1369-70 n.8.

79. *See id.* at 1370.

> if a law changes or abrogates interest payments explicitly provided by the contract, such a law would impair the contractual rights of the parties; whereas, if a law merely changes the amount of interest provided by law as a remedy for breach of the contract, the underlying contract is not necessarily impaired.[80]

The court rejected Trail Mountain's argument, based upon the United States Supreme Court's ruling in *General Motors Corp. v. Romein,*[81] that the statutory prejudgment interest rate had been incorporated into the Agreement when it was signed in 1965. Trail Mountain quoted *Romein*, reminding the court that "state laws are implied into private contracts regardless of the assent of the parties only when those laws affect the validity, construction, and enforcement of contracts."[82] The court reasoned that the statutory prejudgment interest rate did not fit into the narrow category of incorporated statutory provisions discussed in *Romein* because the changes in interest rates promulgated by the state "simply affected the calculation of the remedy granted for a breach of the terms of the lease."[83]

Thus, "in light of [its] holding in *Consolidation Coal*," the court reversed the court of appeals' ruling that upheld "the trial court's assessment of [six percent] prejudgment interest for the entire balance of Trail Mountain's overdue payments."[84] The court remanded the case with "instructions to assess the properly promulgated Board rates of prejudgment interest and penalties for the period during which they were applicable."[85]

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80. *Id.* at 1370. *But see* General Motors Corp. v. Romein, 503 U.S. 181, 189 (1992) (explaining that "state laws are implied into private contracts regardless of the assent of the parties" when they affect the "construction, and enforcement of contracts").

81. 503 U.S. 181 (1992).

82. *Id.* at 189.

83. *Trail Mountain*, 921 P.2d at 1370. The court continued, positing:

> Laws dictating the particular rate of prejudgment interest on delinquent sums are not vested contractual rights. Adjustments in the interest rate, so long as they are not unreasonably punitive, do not "convert an agreement enforceable at law into a mere promise"; nor do they "impair the obligation of pre-existing contracts." So long as the remedy of prejudgment interest is made available in a reasonable form and under appropriato circumstances, parties to a contract are not entitled to assume that one particular rate will predominate or that one particular legal provision governing its assessment will triumph over another.

Id. at 1370-71 (quoting *Romein*, 503 U.S. at 189).

84. *Id.* at 1371.

85. *Id.*

V. ANALYSIS OF THE UTAH SUPREME COURT'S OPINION

The Utah Supreme Court's determination that Utah's retroactive alteration of prejudgment interest rates did not create a contractual impairment subject to Contract Clause scrutiny was incorrect for two fundamental reasons. First, the decision rested upon the faulty assumption that a statutory prejudgment interest rate does not constitute a contractual obligation. Second, the court mistakenly reasoned that since the agreement contained a "subject to the laws of Utah" provision, the State was free to make alterations to the contract, even if the prejudgment interest rate did constitute part of the contract. This reasoning, if widely followed, will equip states with the unfair ability to nullify the restraining effects of the Contract Clause.

A. *The Court Erred in Determining that the Prejudgment Interest Rate did not Constitute a Contractual Obligation*

In determining whether a state has enacted a substantial impairment of a contract,[86] a court should ask three questions: "[1] whether there is a contractual relationship, [2] whether a change in law impairs that contractual relationship, and [3] whether the impairment is substantial."[87] In explaining these factors, the *Romein* Court noted that "[n]ormally, the first two are unproblematic, and we need address only the third. In this case, however, we need not reach the questions of impairment, as we hold that there was no contractual agreement regarding the specific workers' compensation terms allegedly at issue."[88] The *Trail Mountain* court reached essentially the same conclusion. As the paragraphs below explain, however, the state action upheld in *Romein* differed substantially from that upheld in *Trail Mountain*.

In applying this analysis, the *Trail Mountain* court erred in concluding that Utah's retroactive alteration of prejudgment

86. This is the threshold question asked in all Contract Clause challenges. *See Romein*, 503 U.S. at 186 ("Generally, we first ask whether the change in state law has 'operated as a substantial impairment of a contractual relationship.'" (quoting Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 244 (1978))); *accord* Energy Reserves Group, Inc. v. Kansas Power & Light Co., 459 U.S. 400, 411 (1983).

87. *Romein*, 503 U.S. at 186. *See supra* text accompanying notes 23-25.

88. *Id.* at 186-87.

interest rates did not alter a contractual term.[89] The court mistakenly reasoned that since the statute prescribing prejudgment interest rates (in force at the time the Agreement was signed) provided a legal remedy "simply affect[ing] the calculation of the remedy granted for a breach of the terms of the lease,"[90] it did not constitute an operative term of the Agreement.[91]

1. The statute created an implied contractual term

a. Plain language. First, the wording of the statute itself suggested that the prejudgment interest rate it prescribed would be incorporated into all contracts whose terms did not specify another rate. Specifically, the law provided that "[u]nless parties to a lawful contract specify a different rate of interest, the legal rate of interest for the loan or forbearance of any money, goods, or chose in action shall be 6% per annum."[92] Thus, parties entering into a contract in a state where such a provision is in place could reasonably believe that "the legal rate of interest" for any debt accrued under the contract "shall be 6% per annum," and therefore read the statutory prejudgment interest prescription as a contractual obligation.[93]

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89. *See Trail Mountain*, 921 P.2d at 1370-71. The court skillfully euphemized its decision, summarily concluding that as long as the Division was authorized under state law to impose the interest rate, no constitutional provision existed. The court posited that "when the Division sought to enforce the interest and penalty measures promulgated by the Board, it was merely acting pursuant to a right it held under the contract, and no contractual term of the Lease was impaired." *Id.* at 1370.

90. *Id.* at 1370. The court added that

> [a]s a matter of public policy, an award of prejudgment interest simply serves to compensate a party for the depreciating value of the amount owed over time and, as a corollary, deters parties from intentionally withholding an amount that is liquidated and owing. Laws dictating the particular rate of prejudgment interest on delinquent sums are not vested contractual rights.

Id. at 1370-71.

91. *See id.* at 1370-71 ("[T]here is a critical difference 'between interest provided for by contract and interest provided as damages.'" (quoting Consolidation Coal Co. v. Utah Div. of State Lands & Forestry, 886 P.2d 514, 528 n.2 (Utah 1994))).

92. UTAH CODE ANN. 15-1-1(2) (1953).

93. The simplicity of the Supreme Court's most recent discussion of retroactivity is enlightening here. In *Landgraf v. U.S.I. Film Products*, 511 U.S. 244 (1994), the Court explained that retroactive legislation "'attaches new legal consequences to events completed before its enactment.'" *Id.* at 269 n.23 (quoting Miller v. Florida, 482 U.S. 423, 430 (1987)). Inasmuch as the application of the 1953 prejudgment interest statute to the agreement constituted a completed event for purposes of the contract, Utah's subsequent alteration of it was retroactive, and therefore subject to Contract Clause scrutiny.

b. Supreme Court precedent. This interpretation of the prejudgment interest statute is also consistent with the Supreme Court's Contract Clause jurisprudence. The Court has long recognized that "'the laws which subsist at the time and place of the making of a contract . . . enter into and form a part of it.'"[94] Therefore, it stands to reason that laws specifically designed to fill gaps in a contract fit within the definition of "laws which subsist at the time . . . of the making of the contract"[95] and should be considered a contractual provision.[96]

Furthermore, the Supreme Court has recognized that default prejudgment interest rate statutes are in fact incorporated into contracts. In *Von Hoffman v. City of Quincy*,[97] the Court explained:

> This principle embraces alike those [laws] which affect [a contract's] validity, construction, discharge, and enforcement. *Illustrations of this proposition are found, in the obligations of the debtor to pay interest in the maturity of the debt, where the contract is silent.... These are as much incidents and conditions of the contract as if they rested upon the basis of a distinct agreement.*[98]

94. Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 429-30 (1934) (quoting Von Hoffman v. City of Quincy, 71 U.S. (4 Wall.) 535, 550 (1866)).

95. *Id.*

96. *See, e.g.*, Nieves v. Hess Oil Virgin Islands Corp., 819 F.2d 1237, 1244 (3d Cir. 1986) ("The obligations of a contract long have been regarded as including not only the express terms but also the contemporaneous state law pertaining to interpretation and enforcement."); *In re* La Fortune, 652 F.2d 842, 846 (9th Cir. 1981) ("[T]he laws which existed at the time the contract was entered into and which affect its validity, construction, discharge and enforcement, in effect, are incorporated within the contract."); Caritas Servs., Inc. v. Department of Social & Health Servs., 869 P.2d 28, 36 (Wash. 1994) ("Parties are generally deemed to contract in reliance on existing law." (citing Margola Assocs. v. City of Seattle, 854 P.2d 23, 39 (Wash. 1993))); Association of Surrogates and Supreme Court Reporters v. State, 588 N.E.2d 51, 53 (N.Y. 1992) (explaining that laws existing at the time of contracting are "incorporated into them and continued as part of the agreement until new agreements were executed"); Wynne v. New Orleans Clerks and Checkers Union, Local 1497, 550 So. 2d 1352, 1354 (La. Ct. App. 1989) ("'It is a fundamental principle that laws existing at the time a contract is entered into are incorporated into a contract and form a part of the contract as though expressly written therein.'" (quoting Board of Comm'rs v. Department of Natural Resources, 496 So. 2d 281, 294 (La. 1986))); State *ex rel.* Cannon v. Moran, 331 N.W.2d 369, 374 (Wis. 1983) ("Courts have long recognized that under the contract clause a contract includes the laws existing at the time it was made.").

97. 71 U.S. (4 Wall.) 535, 550 (1866).

98. *Id.* (emphasis added).

Thus, the Court noted, without using the precise term, that prejudgment interest statutes are themselves operative contractual provisions.

c. The Court's recent pronouncement in Romein. As the Court recently noted in *General Motors Corp. v. Romein*,[99] the principle that prejudgment interest statutes are operative contractual provisions remains true today. In that case, the Court explained that state actions affecting "the validity, construction, and enforcement of contracts" are implied into contracts "regardless of the assent of the parties."[100] Since prejudgment interest statutes affect the "construction" of contracts, incorporating (if otherwise absent) contractual terms that specify the rate at which interest is to be calculated when one party breaches, the *Romein* decision demands that retroactive alteration may invoke Contract Clause scrutiny.

2. The Trail Mountain *opinion was born out of a fundamental misreading of* Romein

The *Trail Mountain* court's conclusion that the prejudgment interest statute did not constitute a contractual term was founded in part on the fact that the statute "simply affected the calculation of the remedy granted for a breach of the terms [of the agreement]."[101] The court all but concluded that this constituted the beginning and the end of the analysis. This reasoning was supposedly justified because, in the words of the court,

> if a law changes or abrogates interest payments explicitly provided by the contract, such a law would impair the contractual rights of the parties; whereas, if a law merely changes the amount of interest provided hy law as a remedy for breach of the contract, the underlying contract is not necessarily impaired.[102]

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99. 503 U.S. 181 (1992).

100. *Id.* at 189. *See also* McCracken v. Hayward, 43 U.S. (2 How.) 608, 612 (1844) ("The obligation of a contract consists in its binding force on the party who makes it. This depends on the laws in existence when it is made; these are necessarily referred to in all contracts, and forming a part of them as the measure of the obligation to perform them by the one party, and the right acquired by the other. . . . If any subsequent law affect to diminish the duty, or to impair the right, it necessarily bears on the obligation of the contract . . .").

101. *Trail Mountain*, 921 P.2d at 1370.

102. *Id.* at 1370 (citing Morley v. Lake Shore & Mich. S. Ry., 146 U.S. 162, 168-71 (1892)). Ironically, the court cited *Morley* in support of this proposition in blatant

a. Laws providing contractual remedies. The Utah Supreme Court's reasoning stemmed in part from a general misunderstanding of the analysis in the *Romein* opinion. After conceding that *Romein* "observed that not all laws affecting contractual remedies (as opposed to those *directly impairing* contractual rights) will survive Contract Clause scrutiny,"[103] the court appeared to retreat from its concession, suggesting that the *Romein* Court intended "a much more limited holding" which provides little, if any, protection for "laws affecting contractual remedies."[104]

A "careful examination of *Romein*"[105] reveals just the opposite conclusion. Explaining that laws governing contractual remedies are often protected by the Contract Clause, the Court explained that "state laws are implied into private contracts regardless of the assent of the parties" whenever they "affect the validity, construction, and enforcement of contracts."[106] The Court added that laws governing remedies for contractual breach often fit into this category because

> [a] change in the remedies available under a contract, for example, may convert an agreement enforceable at law into a mere promise, thereby impairing the contract's obligatory force. For this reason, changes in the laws that make a contract legally enforceable may trigger Contract Clause scrutiny if they impair the obligation of pre-existing contracts, even if they do not alter any of the contracts' bargained-for terms.[107]

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disregard to the fact that *Morley* held that statutorily prescribed *post*-judgment interest rates are not protected by the Contract Clause. A more careful reading of *Morley* reveals that its holding had no bearing on the merits of *Trail Mountain*, since the Court in *Morley* explained that statutorily imposed post-judgment interest rates are not protected by the Contract Clause because the obligation requiring payment of post-judgment interest stems not from a contract, but from the judgment of a court, and "'[a] judgment is, in no sense, a contract or agreement between the parties.'" *Morley*, 146 U.S. at 169 (quoting Wyman v. Mitchell, 1 Cow. 316, 321 (1823)). Thus, while at first glance *Morley* may appear to contradict strong precedent that certain "state laws are implied into private contracts regardless of the assent of the parties," *Romein*, 503 U.S. at 189, further analysis reveals that it has no bearing on the Contract Clause protection to which statutorily imposed prejudgment interest rates are entitled.

103. *Trail Mountain*, 921 P.2d at 1370 (citing *Romein*, 503 U.S. at 139) (emphasis added).

104. *Id.*

105. *Id.*

106. *Romein*, 503 U.S. at 189 (citing United States Trust Co. of N.Y. v. New Jersey, 431 U.S. 1, 19 n.17 (1977)).

107. *Romein*, 503 U.S. at 189 (citations omitted).

This analysis cannot be squared with the Utah Supreme Court's conclusions. In *Trail Mountain*, the court summarily concluded that because the prejudgment interest rate statute "simply affected the calculation of the remedy," it "did not affect the 'validity, construction, [or] enforcement' [of the agreement],"[108] and therefore was not incorporated into the agreement for Contract Clause purposes. This analysis completely bypassed the guidance given in *Romein*, which was that laws governing the remedies available under a contract *are* often incorporated into contracts because in many instances their alteration can "affect the validity, construction, and enforcement of contracts," thus "trigger[ing] Contract Clause scrutiny . . . even if they do not alter any of the contracts' bargained-for terms."[109] No matter how one reads the Court's opinion in *Romein*, the *Trail Mountain* court's conclusion simply does not follow from it.

b. Sidestepping the "validity, construction, or enforcement" analysis. That the court's conclusion does not follow from *Romein* is evidenced by the fact that the court effectively bypassed *Romein's* analysis dealing with whether the change in prejudgment interest rates affected the agreement's "validity, construction, or enforcement" by summarily concluding that it did not. The court's sole analysis on this aspect of the question consisted of the following sentences:

> In this case, the regulations which altered the rate of prejudgment interest over time did not affect the "validity, construction, [or] enforcement" of the contract between Trail Mountain and the Division. Rather, the regulations simply affected the calculation of the remedy granted for a breach of the terms of the lease. As a matter of public policy, an award of prejudgment interest simply serves to compensate a party for the depreciating value of the amount owed over time and, as a corollary, deters parties from intentionally withholding an amount that is liquidated and owing. Laws dictating the particular rate of prejugment interest on delinquent sums are not vested contractual rights. Adjustments in the interest rate, so long as they are not unreasonably punitive, do not "convert an agreement enforceable at law into a mere promise"; nor do they "impair the obligation of pre-existing contracts." So long as the remedy of prejudgment interest is made available in a reasonable form

108. *Trail Mountain*, 921 P.2d at 1370 (quoting *Romein*, 503 U.S. at 189).
109. *Romein*, 503 U.S. at 189.

> and under appropriate circumstances, parties to a contract are not entitled to assume that one particular rate will predominate or that one particular legal provision governing its assessment will triumph over another.[110]

As the above quote demonstrates, the court's analysis of whether the change in interest rates affected the validity, construction, or enforcement of the Agreement consisted of little more than a drawn-out restatement of the (principally unfounded) conclusion that it did not. This placed undue importance on the distinction between terms "explicitly provided by the contract" and those "provided by law as a remedy for breach of the contract."[111] The *Romein* opinion downplays the importance of this distinction, pointing out that the important question is whether the change in law affects the contract's validity, construction, and enforcement.

c. Factual distinctions. Furthermore, *Romein* can be fairly read as doing nothing more than rejecting General Motors' erroneous argument that "all state regulations are implied terms of every contract entered into while they are effective, especially *when the regulations themselves cannot be fairly interpreted to require such incorporation.*"[112] But even to the extent that it can be read more broadly, two significant factual distinctions reveal that *Romein* did not mandate, or even justify, the result in *Trail Mountain*.

First, the law altered in *Romein* clearly fell outside the category of statutes that could be "fairly interpreted to require such incorporation" because, as the Court observed, it did not supply contractual terms.[113] Indeed, *Romein's* central holding was based in part upon the fact that General Motors was unable to demonstrate that "the alleged right to rely on past payment periods as closed was part of Michigan law at the time of the original contract" and Michigan law did not "explicitly imply a contractual term allowing an employer to depend on the closure of past disability compensation periods."[114] In contrast, Utah's prejudgment interest rate statute by its own terms[115] gave parties to certain

110. *Trail Mountain*, 921 P.2d at 1370-71 (quoting *Romein*, 503 U.S. at 189).

111. *Id.* at 1370.

112. *Romein*, 503 U.S. at 189 (emphasis added).

113. *Id.*

114. *Id.* at 188.

115. UTAH CODE ANN. § 15-1-1(2) (1953) ("Unless the parties to a lawful contract

contracts the justified expectation to rely on a six percent prejudgment interest rate. Therefore, unlike General Motors, Trail Mountain had the right to "explicitly imply a contractual term allowing [it] . . . to depend on [the prejudgment interest rate supplied by the statute]."[116]

Second, the *Romein* Court justified its conclusion on the fact that "[t]he employment contracts at issue were formed before the [earlier statute that General Motors claimed was incorporated into the contracts] came into effect."[117] By contrast, the statute involved in *Trail Mountain* was in effect at the time the parties signed the Agreement. The *Trail Mountain* court therefore erred in assuming that the statutory alteration was entitled to as much deference as the statute in *Romein* was awarded. The *Romein* opinion stands for the position that a state may not rely on its own laws to alter its own contractual obligations.[118]

Therefore, in concluding that retroactive changes in Utah's prejudgment interest statute are not subject to Contract Clause scrutiny, the *Trail Mountain* court fundamentally misconstrued and misapplied the Court's opinion in *Romein*. The court thereby implicitly concluded that Contract Clause questions are to be decided according to state law, instead of federal constitutional law.

B. The Trail Mountain *Court Erred in Relying on the Deference to the State Law Provision in the Agreement*

The Utah Supreme Court was also incorrect in holding that the State's retroactive alteration of the prejudgment interest rate was justified under the terms of the agreement itself. The court postulated that since the agreement contained a provision explaining that it was "expressly subject to the laws of Utah," Trail Mountain's predecessor explicitly submitted itself to the possibility that the State could unilaterally alter the prejudgment interest rate at any time.[119] The court's reasoning would suggest that the State, by including similar provisions in all of

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specify a different rate of interest, the legal rate of interest for the loan or forbearance of any money, goods, or chose in action shall be 6% per annum.").

116. *Romein*, 503 U.S. at 188.

117. *Id.*

118. *See id.*

119. *Trail Mountain*, 921 P.2d at 1369.

its contracts, could change its obligations at any time. In the court's own words:

> Trail Mountain's Lease contained [a provision stating that the Agreement was subject to the laws of Utah], which also expressly stated that the Lease was subject to the rules and regulations promulgated by the Board. Hence, when the Division sought to enforce the interest and penalty measures promulgated by the Board, it was merely acting pursuant to a right it held under the contract, and no contractual term of the Lease was impaired.[120]

This conclusion is constitutionally indefensible because it potentially limits all Contract Clause protections to the often narrower protections of state law.

1. Romein's *dicta*

In *Romein*, the Supreme Court warned against reasoning that a state has the ability to retroactively alter an agreement when an agreement contains a provision that it is expressly subject to state law. Explaining that deciding Contract Clause disputes solely on the basis of state law could lead to the complete evisceration of the Contract Clause, the Court explained that "taken to an extreme, it would render the Contract Clause itself

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120. *Id.* at 1369-70. It is interesting, if not revealing, to note that the court conceded in a footnote that "[o]bviously, there are natural limits to such provisions. The State cannot simply opt out of Contract Clause scrutiny by including such language in all of their contractual agreements and then subsequently rely upon a legislative edict that otherwise clearly violates the Contract Clause." *Id.* at 1370 n.8.

However, the court promptly denied allowing the State to engage in such treachery, asserting:

> [I]n this case we are not dealing with an unanticipated legislative action which abrogates the validity or enforcement of a provision of the contract at issue. Rather, Trail Mountain's Lease specifically provided for . . . regulation[s] . . . that . . . merely prescribed the method of calculating compensation for violation of the terms of the Lease. Hence, the nature and source of the interest and penalty provisions were reasonably foreseeable, and their imposition did not alter any of the essential elements of the contract.

Id. This reasoning is used throughout the court's opinion: if the law authorizes the State to take a certain action (either by statute or contract), that action is not subject to the restraints of the Contract Clause. This is a most novel line of constitutional reasoning.

Furthermore, in no way did the agreement "specifically provide[]," *id.*, that the State could retroactively alter the prejudgment interest rate. At best, such a conclusion is a phenomenal stretch of a provision subjecting a contract to the laws of the State.

entirely dependent on state law."[121] Quoting Justice Story, the Court then noted that this reasoning has long been rejected:

> "If [the idea that the municipal law of the place where a contract is made forms a part of the contract] were admitted to be true, the consequence would be, that all the existing laws of a State, being incorporated into the contract, would constitute a part of its stipulations. . . . If, therefore, the legislature should provide, by a law, that all contracts thereafter made should be subject to the entire control of the legislature, as to their obligation, validity, and execution, whatever might be their terms, they would be completely within the legislative power, and might be impaired or extinguished by future laws; thus having a complete *ex post facto* operation."[122]

Hence, Justice Story and the *Romein* Court warned of the very mischief in which Utah has engaged: allowing a State to limit the Contract Clause to the boundaries of state law. While *Romein* discussed this principle in a slightly different context,[123] the United States Court of Appeals for the Eighth Circuit recently applied the same concept in a very similar context.

2. The Eighth Circuit's Opinion in In re Workers' Compensation Refund

The Eighth Circuit recently confronted a similar dispute, and correctly applied the Supreme Court's Contract Clause jurisprudence. In *In re Workers' Compensation Refund*,[124] the court found that a state action remarkably similar to that involved in *Trail Mountain* violated the Contract Clause. The dispute in *Workers' Compensation Refund* arose after Minnesota retroactively nullified the contractual rights of several insurers to a $302 million workers' compensation reinsurance pool refund. Under contracts

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121. *Romein*, 503 U.S. at 190.

122. *Id.* at 190-91 (quoting 2 JOSEPH STORY, COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES § 1383, at 252-53 (5th ed. 1891)).

123. The *Romein* Court expressed this concern in defense of its explanation that not all provisions of state law are incorporated into contracts. Ironically, while the *Trail Mountain* court relied heavily on selected statements from *Romein* explaining that principle, the above quotations reveal that in reality, those statements undercut the court's own reasoning. The *Romein* opinion could not have been clearer in explaining that state law cannot determine the scope of the Contract Clause. *See Romein*, 503 U.S. at 190-91 (explaining that Contract Clause disputes cannot be decided solely on the basis of state law).

124. 46 F.3d 813 (8th Cir. 1995).

between the insurers and the State, insurers had the right to collect a refund from excess funds in the reinsurance pool.[125] Like the agreement in *Trail Mountain*, the contracts in *Workers' Compensation Refund* contained a provision stating that the contracts would "be deemed to be automatically amended to conform to any amendment" of applicable state law.[126]

Minnesota argued (as unsuccessfully as the Division argued successfully in *Trail Mountain*) that this express provision allowed the State to alter its contractual obligations by amending its applicable laws. Recognizing that this argument could not withstand the United States Supreme Court's Contract Clause scrutiny as articulated in *Romein*, the Eighth Circuit held that Minnesota's action was unconstitutional. The court explained:

> An expansive interpretation of the automatic amendment clause to permit complete retroactive amendment essentially deems all rights or obligations in those contracts illusory, because these rights could always be changed or obliterated. An expansive retroactive application also converts the automatic amendment clause into a blanket waiver of the insurance companies' right to Contract Clause protection. Contractual clauses purporting to waive constitutional rights must be clear and unambiguous.[127]

Thus, the Eighth Circuit held that "retroactive amendment" clauses do not allow a contracting state to avoid Contract Clause scrutiny unless such provisions clearly state that the other party will have no Contract Clause recourse in the event that the state subsequently chooses to alter its obligations.[128]

The *Trail Mountain* opinion is inconsistent with the Eighth Circuit's conclusions in *Workers' Compensation Refund* and with the Supreme Court's Contract Clause jurisprudence in general. In upholding the State's retroactive action, the Utah Supreme Court concluded that by entering into the Agreement, Trail Mountain's predecessor-in-interest executed exactly the same kind of "blanket waiver"[129] of all future Contract Clause protection that was flatly rejected by the Eighth Circuit. Read as a whole *Trail Mountain* suggests that the extent of the protections

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125. *See id.* at 819.
126. *Id.* at 818.
127. *Id.* at 819 (citations omitted).
128. *See id.*
129. *Id.*

granted by the Contract Clause should be determined by state law. This is a novel position, and one that is inconsistent with our constitutional tradition.

VI. CONCLUSION

The logical implication of the *Trail Mountain* opinion is that states can avoid Contract Clause scrutiny altogether by either (1) denying that they altered a contractual provision,[130] or (2) claiming that the challenging party "waived" its rights to Contract Clause protection by signing a contract with the state, which provided that the contract was subject to the laws of that state. If followed, this reasoning could destroy the long-recognized and historically important[131] protections provided by the

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130. If (as in *Trail Mountain*) a state can argue (as Utah did successfully) that default prejudgment interest rate statutes do not constitute contractual provisions and are therefore not subject to Contract Clause scrutiny because in the opinion of the State they do not affect the validity, construction, or enforcement of contracts, then it can safely be said that *no* state laws are *ever* incorporated into contracts, and their alteration *never* invokes the scrutiny of the Contract Clause. While this may be appealing to states, it contradicts the Supreme Court's most recent discussions of the Contract Clause, along with 170 years of constitutional jurisprudence before it. *See* General Motors Corp. v. Romein, 503 U.S. 181, 189 (1992) ("[C]hanges in the laws that make a contract legally enforceable may trigger Contract Clause scrutiny if they impair the obligation of pre-existing . . . contracts' bargained-for terms.").

131. One can hardly discount the importance that the Framers placed on the Contract Clause. On several different occasions, James Madison discussed the profound importance of the Contract Clause. In THE FEDERALIST NO. 10, he explained that "the protection of [the] faculties of acquiring property" is "the first object of government," suggesting that states had a higher obligation to refrain from interfering with contracts than almost anything else. THE FEDERALIST NO. 10, at 58 (James Madison) (Jacob E. Cooke ed., 1961).

Madison was always skeptical of the ability of the states to legislate retroactively. He once cautioned about the danger of "[t]he mutability [sic] of the laws of the States," adding that the potential unpredictability created by constantly fluctuating state law "contributed more to that uneasiness which produced the Convention" than other concerns. Letter from James Madison to Thomas Jefferson (Oct. 24, 1787), *in* 5 THE WRITINGS OF JAMES MADISON 17, 27 (Gaillard Hunt ed., 1904). He echoed the same concern in THE FEDERALIST NO. 44. As he explained:

> The sober people of America are weary of the fluctuating policy which has directed the public councils. They have seen with regret and with indignation, that sudden changes and legislative interferences in cases affecting personal rights, become jobs in the hands of enterprising and influential speculators; and snares to the more industrious and less informed part of the community.

THE FEDERALIST NO. 44, at 301 (James Madison) (Jacob E. Cooke ed., 1961).

Madison was not alone in his belief in the paramount importance of the Contract Clause. Alexander Hamilton once commented that a State's attempts to limit its own contractual obligations "may be safely said to be a contravention of the first principles of natural justice and social policy . . . ." BENJAMIN FLETCHER WRIGHT, JR., THE CONTRACT CLAUSE OF THE CONSTITUTION 22 (1938).

Contract Clause. This would be a constitutionally unacceptable result.

In spite of the fact that the United States Supreme Court denied certiorari in *Trail Mountain*,[132] those concerned about the future of the Contract Clause can perhaps take comfort in the fact that the *Trail Mountain* opinion itself may have set in motion a sequence of events that will ultimately lead to its own jurisprudential destruction.[133] As more courts consider issues similar to those involved in *Trail Mountain*, inevitably, some will adopt the Utah Supreme Court's reasoning and others will reject it (as evidenced by the Eighth Circuit's decision in *Workers' Compensation Refund*), creating a split of authority. Indeed, *Worker's Compensation Refund* and *Trail Mountain* show that such a split already exists. Ultimately, this split could convince the Supreme Court to grant certiorari in a future, similar case and provide the Court with an opportunity to clarify its opinion in *Romein* and bolster the currently weakened Contract Clause.

In the meantime, it will be interesting to observe whether other states will create similar loopholes in the Contract Clause. To the extent that they do, they will send the constitutionally indefensible message to the public (especially private parties who enter into contracts with government entities) that states are unlike other entities in that they have the unique ability to retroactively alter their own contracts without penalty.

From a practical standpoint, the *Trail Mountain* holding will have far-reaching, detrimental consequences. For example, when private parties enter into contracts with a state, they will be fearful of the State's ability (following the *Trail Mountain* line of reasoning) to later amend or limit its own obligations under those contracts. Acting under this fear, private contractors will be forced to demand more favorable terms to offset the risk of doing business with the only kind of entity that can unilaterally and retroactively alter its own contracts. Thus, States will have to pay more money for the same services (e.g., when hiring road construction contractors) and receive less money for the same privileges (e.g., when executing mining leases) whenever they enter into contracts with private parties. In time, states will

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132. *See* 117 S. Ct. 1017 (1997) (denying Trail Mountain's petition for certiorari).

133. This is not to say that the precise holding of *Trail Mountain* could be reversed by future Supreme Court review, but simply that its logical foundation certainly could be.

inevitably either (1) be forced to raise taxes in order to provide the more favorable contractual terms that private parties will demand, or (2) make retroactive contractual alterations even more drastic than those involved in *Trail Mountain*, thereby making private contractors even more hesitant to do business with a state.

The optimist could argue that *Trail Mountain* presented a unique set of facts and that, even if widely followed, its holding would have limited, if not insignificant, application. The breadth and depth of the opinion suggests that a state may redefine its own contractual obligations through retroactive legislation and regulation, regardless of the context.[134] However, even if the *Trail Mountain* analysis is only followed with respect to the relatively discrete area of prejudgment interest statutes, its effects will be anything but insignificant. As Trail Mountain argued to the United States Supreme Court in its Petition for Certiorari:

> There is also grave danger that—absent review—the Contract Clause will be seriously debilitated beyond the borders of Utah. The Utah Supreme Court's analysis not only conflicts with decisions from this and other courts, it could well serve as a hornbook for future "creative avoidance" of the Contract Clause in other jurisdictions. Every state in the nation has a prejudgment interest statute that operates similarly to [Utah's]. Numerous states, furthermore, manage public trust properties under obligations to obtain full (or fair) value upon their disposition. The decision below—by demonstrating how prejudgment interest statutes can be ignored and public trust responsibilities exploited—is an enticing outline for the constitutionally effective rewriting of thousands of contracts held by financially strapped States.[135]

Thus, to say that the *Trail Mountain* line of reasoning may only apply to cases involving retroactive alteration of prejudgment interest rates is not to say that such application will be of little consequence. If the Utah Supreme Court's decision in *Trail Mountain* is widely followed, innumerable private parties doing business with states stand in grave jeopardy of having their contractual guarantees severely curtailed.

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134. *See Trail Mountain*, 921 P.2d at 1369-70 (upholding Utah's retroactive contractual alterations against a Contract Clause attack on grounds that the alteration was justified by state law).

135. Trail Mountain's Petition for Certiorari at 17-18, *Trail Mountain* (No. 96-775).

In the end, the states will undoubtedly see the negative practical consequences of "Trail-Mountainizing" their own contractual obligations. Perhaps this will be enough to convince them to avoid engaging in such chicanery. If not, perhaps the courts will see the important constitutional implications and recognize that, since the Contract Clause does not allow the states to "trick a group of individuals into parting with money on one set of conditions only to find that it is bound by another,"[136] the Utah Supreme Court's opinion in *Trail Mountain* was constitutionally indefensible.

Michael S. Lee

136. Richard A. Epstein, *Toward a Revitalization of the Contract Clause*, 51 U. CHI. L. REV. 703, 720-21 (1984).