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Determination of Property Rights in Public Contracts after Winstar v. United States: Where has the Supreme Court Left Us, The

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The Determination of Property Rights in Public Contracts after *Winstar v. United States*: Where has the Supreme Court Left Us?

INTRODUCTION

In the summer of 1996, the long tangled road of litigation between a group of financial institutions and the United States government reached its apex with the Supreme Court's decision in *United States v. Winstar*.[1] In *Winstar*, the Supreme Court was asked to decide whether Congress' enactment, and the agencies' subsequent enforcement, of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA)[2] had breached contracts between the financial institutions and the government.[3] FIRREA imposed uniform regulatory requirements on the thrift industry, thus abrogating government contractual promises of special regulatory treatment, which the government had made as an inducement for healthy thrifts to merge with financially insolvent thrifts in order to prevent a wholesale collapse of the savings and loan industry. Affirming the decision of the appellate court, the Supreme Court held, in a divided decision, that the government had assumed the risk of future regulatory change and was thus liable to the financial institutions for breach of contract.[4]

In examining the contracts entered into between the banks and the government, the Supreme Court was called upon to evaluate a number of defenses offered by the government, most notably the "unmistakability doctrine" and the "sovereign acts doctrine." The significance of the Supreme Court's decision lies in its treatment of these sovereign defenses and the uncertainty the three-part majority decision portends for future practitioners in evaluating government contracts. Most importantly, *Winstar*

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1. United States v. Winstar Corp., 518 U.S. 339, 116 S. Ct. 2432 (1996).
2. Financial Inst. Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (codified as amended in scattered sections of U.S.C.).
3. *Winstar*, 116 S. Ct. at 2447-48.
4. *Id.* at 2440.

represents a potentially enormous contraction of the government's traditional reserved sovereign authority over federally created property rights. This article will examine the Court's reasoning and show how it essentially misinterprets previous decisions of the Court regarding the role of federal sovereign power in interpreting government contracts. The article will conclude by arguing that such a judicial shift should occur only where these consequences are understood and fully argued in their proper context.

BACKGROUND

During the Great Depression, the high number of failures in the savings and loan industry prompted Congress to pass several statutes designed to stabilize the banks, and savings and loans of the thrift industry.[5] Pursuant to these statutes Congress created the Federal Home Loan Bank Board (Bank Board) to charter and regulate federal thrifts and the Federal Savings and Loan Insurance Corporation (FSLIC) to insure thrift deposits.[6] These institutional regulatory structures stabilized the industry until high interest rates and inflation in the late 1970s and early 1980s brought on a new round of thrift failures.[7] In response, laws were passed by both Congress and various states easing regulatory controls on the thrifts, including the lowering of the capital reserve levels historically required to protect thrifts from unanticipated loan defaults.[8] In an effort to avoid depleting the insurance assets of the FSLIC, the Bank Board encouraged healthy thrifts to take over failing institutions pursuant to special contracts known as "forbearance agreements."[9] As an incentive to enter into these agreements, the Board offered the healthy thrifts favorable accounting treatments, which allowed the acquiring institutions to maintain a positive account balance and to leverage more loans, despite the liabilities of their new thrift assets.[10] Despite these efforts, thrifts continued to fail and the

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5. *See* Transohio Savings Bank v. Dir., Office of Thrift Supervision, 967 F.2d 598, 601 (D.C. Cir. 1992). The statutes include the Federal Home Loan Bank Act, 12 U.S.C. §§ 1421-49 (1994); Home Owner's Loan Act, 12 U.S.C. §§ 1461-68c (1994); and the National Housing Act, 12 U.S.C §§ 1701-50g (1994).

6. Federal Home Loan Bank Act, 12 U.S.C. §§ 1421-49 (1994).

7. *See Winstar*, 116 S. Ct. at 2440.

8. *See id.* at 2440-46. In November 1980, the capital reserves requirements were lowered from five percent of total assets to four percent, and to three percent in January 1982. *See id.*, at 2441.

9. *See* David B. Toscano, *Forbearance Agreements: Invalid Contracts for the Surrender of Sovereignty*, 92 COLUM. L. REV. 426, 453, n.133 (1992); Sterling Sav. Ass'n v. Ryan, 751 F. Supp. 871, 873 (E.D. Wash. 1990).

10. *See Winstar*, 116 S. Ct. at 2442. The essence of this favorable accounting treatment were the provisions in most forbearance agreements that allowed the acquiring thrift institution to treat the net liabilities of the failing thrifts (fair market value of assets minus

FSLIC became insolvent by 1988.[11]

In response to the growing crisis, Congress passed FIRREA in 1989. FIRREA abolished the Bank Board and the FSLIC and replaced these agencies with the Office of Thrift Supervision (OTS). FIRREA also enacted new, uniform capital standards that replaced the variable standards promulgated by the Bank Board, including the favorable accounting treatments agreed to in the various forbearance agreements.[12] As a result of new regulations established by the OTS pursuant to the standards set forth in FIRREA, many previously solvent thrifts fell out of compliance with federal reserve requirements, thus becoming targets of federal sanctions, including prohibitions on asset growth and potential seizure by OTS officials.[13]

Winstar began as two separate lawsuits brought in the federal claims court by three thrifts who had entered into forbearance agreements with the Bank Board, only to see their accounting preferences eliminated by FIRREA, leading to financial upheaval and, for two of the thrifts, federal seizure.[14] After reviewing the thrifts' breach of contract claims, the court

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overall liabilities) as "supervisory goodwill." *Id.* at 2443; Toscano, *supra*, note 9, at 428–29. As explained by Justice Souter, supervisory goodwill was attractive to healthy thrifts for several reasons. First, the agreements allowed the acquiring thrifts to count supervisory goodwill toward their reserve requirements; this treatment increased the thrift's reserve accounts "thereby allowing the thrift to leverage more loans (and . . . more profits)." *Winstar*, 116 U.S. at 2443. Second, the healthy thrifts were permitted to amortize the supervisory goodwill over long periods ranging typically from 25 to 40 years. *Id.* at 2443; Toscano, *supra* note 9, at 430. Because these amortization terms greatly exceeded the terms of loan agreements whose discounts could be counted as capital gains, the acquiring thrifts could actually show a net paper profit in the initial years following the merger. *See generally Winstar*, 116 S. Ct. at 2444 for a more detailed description of this accounting procedure. Finally, in agreements in which the FSLIC contributed cash subsidies as a further inducement towards merger, the acquiring thrift was not required to reduce the amount of calculated supervisory goodwill, thus conferring, in effect, a double counting of the cash received as a tangible and an intangible asset. *Id.* at 2444, *citing Transohio*, 967 F.2d at 604.

11. *Winstar*, 116 S. Ct. at 2441.

12. *See Winstar*, 116 S. Ct. at 2446–47; *see* Toscano, *supra*, note 9, at 430-31.

13. In response to the enactment of FIRREA, the OTS directed savings associations to eliminate all favorable accounting treatments conferred under the forbearance agreements in determining whether or not they comply with the new minimum regulatory capital standards. *See Winstar*, 116 S. Ct. at 2446; Financial Inst. Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (codified as amended in scattered sections of U.S.C. (FIRREA); *see also* Sterling Sav. Ass'n v. Ryan, 751 F. Supp. 871, 875–76 (E.D. Wash. 1990), *vacated*, 959 F.2d 241 (9th Cir. 1992); Far West Fed. Bank v. Director, Office of Thrift Supervision, 738 F. Supp. 1564, 1568 (D. Or. 1990), *rev'd*, 951 F.2d 1093 (9th Cir. 1991).

14. The three thrifts were Glendale Federal Bank, Winstar Corporation and The Statesman Group, Inc. While Glendale was able to recapitalize following passage of FIRREA, Winstar and Statesman were both seized and liquidated by federal regulators. *Winstar*, 116 S. Ct. at 2447.

found that the government had breached each of the respective forbearance agreements by enacting and enforcing FIRREA.[15] The claims court then certified the cases for interlocutory appeal. The appellate court reversed, in a divided decision, holding that the government had never made an "unmistakable" promise not to change the regulatory standards set forth in the forbearance agreements, and thus had not breached those agreements by imposing the new FIRREA standards on the thrifts.[16] Upon a rehearing, the en banc court reversed this decision, essentially adopting the claims court's analysis that the government had breached its contractual obligation to provide favorable regulatory treatment and thus was liable to the thrifts for damages.[17] The Supreme Court upheld the appellate court's decision, finding by a seven to two majority that, in executing the forbearance agreements with the thrifts, the government had assumed the risk of future regulatory change and was thus liable for any damages that flowed from the enactment of FIRREA.[18]

SUPREME COURT'S DECISION IN *WINSTAR*

*Winstar*is a difficult decision to decipher due to the three separate opinions that purport to represent the seven justice majority. Justice Souter authors the main opinion, which is joined by Justices Stevens, O'Conner and Breyer.[19] Justice Breyer adds a separate concurrence.[20] Justice Scalia offers his own opinion, joined by Justices Kennedy and Thomas, who concurs in the judgment, but not the reasoning, of the main opinion.[21] Justice Rhenquist

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15. *See* Winstar Corp. v. United States, 21 Cl. Ct. 112 (1990) [hereinafter Winstar I]; Winstar Corp. v. United States, 25 Cl. Ct. 541 (1992) [hereinafter Winstar II]; Statesman Sav. Holding Corp. v. United States, 26 Cl. Ct. 904 (1992). In so holding, the Federal Claims Court rejected the reasoning of the D.C. Court of Appeals in *Transohio*, 967 F.2d 598 (D.C. Cir. 1992), which had reviewed similar agreements and found the government not liable on related statutory and due process claims. *Statesman*, 26 Cl. Ct. at 916-23. The findings and reasoning of the Federal Claims Court in making these decisions will be discussed, where appropriate, later in this article.

16. *See Winstar Corp. v. United States*, 994 F.2d 797, 810 (Fed. Cir. 1993).

17. *See Winstar Corp. v. United States*, 64 F.3d 1531, 1540, 1545 (Fed. Cir. 1995).

18. *See Winstar*, 116 S. Ct. 2432; *infra* notes 21-55 and accompanying discussion for a description of the Court's reasoning in finding for the thrifts.

19. *See Winstar*, 116 S. Ct. at 2459. Justice O'Conner does not join in part IV of Justice Souter's opinion, which addresses the sovereign acts doctrine.

20. *See id.*

21. *See id.* This article will normally refer to each opinion according to their three respective authors, Souter, Breyer and Scalia. From time to time the article may refer to Justice Souter and Justice Breyer's opinion as the "majority opinion" despite the fact that only 4 out of 9 Justices stood behind its reasoning. The collective decision of the seven member majority—which includes the opinions of Souter, Breyer and Scalia—may be attributed occasionally to the "Court."

writes a dissent, which is joined by his ideological opposite, Justice Ginsburg.[22]

Justice Souter's opinion begins by examining the underlying contracts between the government and the thrifts. The opinion finds that the government made a promise to contractually extend favorable regulatory treatment to each of the thrifts.[23] Justice Souter notes that the language of the agreements, though lacking optimum clarity, appears to "lock in" this favorable regulatory treatment.[24] Based on this interpretation of the contractual documents, the opinion upholds the lower court's ruling that the government breached its respective obligations to each of the thrifts by enacting and subsequently implementing the uniform regulatory treatment required by FIRREA.[25] The opinion then addresses whether the Government could successfully assert any of its four defenses to the thrifts' breach of contract claims.[26]

The first of these defenses is known as the unmistakability doctrine. The unmistakability doctrine states that "sovereign power, even when unexercised, is an enduring presence that governs all contracts subject to the sovereign's jurisdiction, and will remain intact unless surrendered in unmistakable terms."[27] Based on this doctrine, the government argued that the forbearance contracts should not be construed as limiting the government's power to impose new regulatory restrictions on the thrifts since the government had not made an unmistakable promise to waive its sovereign right to enact legislation in the future.[28] Justice Souter's opinion rejects this

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22. *See id.* Justice Ginsburg does not join in part II of the dissent, which addresses the sovereign acts doctrine.

23. *See id.* at 2452.

24. *Id.* at 2451. Justice Souter makes this conclusion based upon the language of the Assistance Agreement (one of the contract documents), which states that the Bank Board's resolutions and actions in connection with the merger (which adopt the favorable regulatory treatment) shall prevail over contrary regulations and accounting principles. *See id.* A supporting argument not addressed by the Supreme Court was the extent to which the long amortization periods for supervisory goodwill, *see supra* note 10, at indicated the parties' intent that the favorable regulatory treatment would continue into the 21st century.

25. *See Winstar*, 116 S. Ct. at 2452. The opinion notes that "the Government exacerbated its breach when it seized and liquidated [the] respondents' thrifts for regulatory noncompliance." *Id.* at 2453.

26. *Id.* at 2453. As will be shown, the majority opinion's initial finding that the government *breached* the forbearance agreements, without ever applying or even considering the applicability of the unmistakability doctrine to determine the respective rights of the parties to the contracts, represents an error of law that sets the stage for the problems encountered in the rest of the opinion. *See infra* notes 175–94 and accompanying discussion.

27. Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 52 (1986), *quoting* Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 148 (1982), *quoting* St. Louis v. United Rys. Co., 210 U.S. 266, 280 (1908).

28. *Winstar*, 116 S. Ct. at 2453.

argument based upon the reasoning that the unmistakability doctrine is simply not applicable in cases where enforcement of the alleged contractual obligation does not "block the exercise of a sovereign power of the United States."[29] In examining the forbearance contracts, the opinion finds that the government's promise merely acted to shift the liability risk for future regulatory change to the government.[30] Since enforcement of this risk allocation would not bar the government from exercising its sovereign powers, the unmistakability doctrine does not apply.[31]

Justice Souter uses the same reasoning to dispense with two additional defenses raised by the government. The first of these, the reserved powers doctrine, holds that a government may not contract away an essential attribute of its sovereignty.[32] The second, the express delegation doctrine, holds that the delegation of authority to contract away a sovereign power of the government must be clearly made and all doubts must be resolved in favor of the continuance of the power.[33] Neither doctrine is applicable, according to Justice Souter, because the forbearance contracts did not purport to surrender the Government's sovereign power to regulate.[34]

The government's fourth and final defense to the breach of contract claim was based upon the sovereign acts doctrine, which holds that the government, in its capacity as a contractor, may not be held responsible for its acts taken as a sovereign.[35] The purpose of the sovereign acts doctrine is to place the government in the same position as a private contractor, whose liability for unforeseen government actions would be determined according

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29. *Winstar*, 116 S. Ct. at 2457. According to Justice Souter, the question of whether an alleged contractual term may have the effect of blocking the exercise of sovereign authority may be answered by examining the language of the underlying contractual agreement. *Id.* at 2457 n.24. One theme of this article is that this question is more likely to be answered by the remedy sought by the private party. *See infra* notes 155–77 and accompanying text. For that reason, this article will from time to time refer to Justice Souter's approach for determining whether the unmistakability doctrine should apply as the "remedy test."

30. *Winstar*, 116 S. Ct. at 2457–58.

31. *Id.* at 2458.

32. United States Trust Co. of New York v. New Jersey, 431 U.S. 1, 23 (1977); Stone v. Mississippi, 101 U.S. 814, 817 (1879). Souter reaches this holding without expressly finding that the reserved powers doctrine applies to the federal government. *See Winstar*, 116 S. Ct. at 2461 (Government's argument that the logic of reserved powers doctrine applies equally to the federal government "may be so but is also beside the point."). *See infra* notes 150–54 and accompanying text for a discussion of how the application of the reserved powers doctrine to the federal government is relevant to a plausible interpretation of the unmistakability doctrine.

33. Home Tel. & Tel. Co. v. City of Los Angeles, 211 U.S. 265, 273 (1908).

34. *Winstar*, 116 S. Ct. at 2462.

35. Horowitz v. United States, 267 U.S. 458, 461 (1925).

to the common law of contract interpretation.[36] Justice Souter rejects the government's sovereign acts defense, however, holding that the government failed to meet the requirements for its successful assertion. First, Souter finds that because FIRREA had a "substantial effect"[37] on the government's own contractual obligations (incurred through the many forbearance agreements entered into during the 1980s), it does not satisfy the requirement that the legislation be a "public and general" act.[38] Second, even if FIRREA were considered to be a public and general act, the government could not avoid liability as a private party since it would not meet the two further requirements under the common law commercial impossibility standard, that the parties 1) neither foresaw the occurrence of the sovereign act; nor 2) addressed such a possibility in the contract.[39] According to Souter, the government would be unable to show that future regulatory change was an unforeseeable event, given the contractual language providing for particular regulatory treatment and given the highly regulated nature of the thrift industry.[40] Moreover, the language of the underlying contracts that allocated the risks of future regulatory change to the government indicated that the parties' performance obligations were not meant to be discharged due to the enactment of new legislation.[41] After rejecting each of the government's defenses, Justice Souter's opinion affirms the lower court's ruling finding the government liable for breach of contract

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36. *Winstar*, 116 S. Ct. at 2463; Jones v. United States, 1 Ct. Cl. 383, 384 (1865).

37. For a discussion of the "substantial effect" test introduced by *Winstar*, 116 S. Ct. 2432, see *infra*, notes 344–54 and accompanying text.

38. *Winstar*, 116 S. Ct. at 2467–69. The opinion states that, although "Congress acted to protect the public in the FIRREA legislation . . . the extent to which this reform relieved the Government from its own contractual obligations precludes a finding that the statute is a 'public and general' act for purposes of the sovereign acts defense." *Id.* at 2469; Financial Inst. Reform, Recovery, and Enforcement Act of 1989, Pub. L. No. 101-73, 103 Stat. 183 (codified as amended in scattered sections of U.S.C.) (FIRREA).

See, e.g., *Horowitz*, 267 U.S. at 461; *Jones*, 1 Ct. Cl. at 384. *See also* Wilson v. United States, 11 Ct. Cl. 514, 520 (1875) (general enactments of Congress are not to be construed as evasions of a particular contract); Deming v. United States, 1 Ct. Cl. 190, 191 (1865).

39. RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981). In other words, the government as private contractor would be entitled, under the sovereign acts doctrine, to argue that its performance had been rendered impossible as a result of the sovereign act.

> [w]here, after a contract is made, a party's performance is made impracticable without his fault by the occurrence of an even the non-occurrence of which was a basic assumption on which the contract was made, his duty to render that performance is discharged, unless the language or the circumstances indicate the contrary. *Id.*

40. *Winstar*, 116 S.Ct. at 2469–70. The opinion supports this holding with transcripts of the government's lawyers stating at oral argument that FIRREA's tightening of the capital standards was "exactly the event that the parties assumed might happen when they made their contracts." *Id.* at 2470 n.54.

41. *Id.* at 2471.

and remands the case for a determination of the appropriate measure of damages.[42]

Justice Breyer's concurrence emphasizes that the unmistakability doctrine should not be applied to ordinary government contracts that allocate risks in the same manner as between two private parties.[43] Breyer rejects the government's claim that the possibility of substantial damage awards carries the danger of limiting the exercise of sovereign power. According to Breyer, this argument has no logical stopping point that would prevent its application to routine government supply contracts, agreements that instead should properly be governed by ordinary principles of contract law.[44]

Justice Scalia's opinion, while concurring with the Court's judgment against the government, differs considerably in its legal analysis. Justice Scalia disagrees that the unmistakability doctrine is not applicable to the forbearance agreements.[45] He rejects the majority opinion's reasoning that the application of the doctrine turns on the nature of the contract at issue, i.e., whether the contractual provisions attempt to bind the legislative powers of the sovereign or whether they merely allocate the monetary risk of future regulatory change.[46] Instead, Justice Scalia characterizes the doctrine as "a rule of presumed intent" that "the sovereign does *not* promise that none of its multifarious acts, needful for the public good, will incidentally disable it or the other party from performing one of the promised acts."[47] According to Scalia, only "unmistakable language" will rebut this presumption. Scalia finds such language in the government's contractual promises to grant the thrifts favorable regulatory treatment.[48]

Without expressly stating, Scalia's opinion implies a close connection between the unmistakability and sovereign acts doctrines. Under Scalia's analysis, the primary function of the unmistakability doctrine is to establish whether the government has waived its right to assert the sovereign acts doctrine as a defense to liability where the government's

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42. *Id.* at 2472.

43. *Id.* at 2472-73. Justice Breyer notes that the doctrine was "not determinative" in the Court's other unmistakability decisions. *Id.* at 2472.

44. *Id.* at 2475.

45. *Id.* at 2477.

46. *Id.* at 2476. Justice Scalia notes that such an approach has no basis in precedent nor does it amount to a real distinction given the fact that all contract cases ultimately come down to monetary liability for one party or another. *Id.*

47. *Id.* at 2477.

48. *Id.* at 2478. Scalia makes this finding as a matter of law based on the lower courts' findings that the government had "plainly made promises to regulate in a certain fashion into the future." *Id.*

sovereign acts have hindered or prevented contractual performance.[49] Accordingly, Scalia rejects the proffered sovereign acts defense based on his earlier finding that the government unmistakably waived this right.[50]

Justice Rhenquist's dissent criticizes the majority opinion's narrowing of the government's sovereign defenses.[51] Rhenquist objects to Justice Souter's remedy test, noting that 1) the distinction between a claim for money damages and a claim to be exempt from the operation of a statute will always be tenuous;[52] and 2) the distinction is not supported by recent Supreme Court decisions that applied the unmistakability doctrine to interpret contract claims for money damages.[53] The dissent points out the illogic of having the application of the unmistakability doctrine turn on the remedy sought for the government's breach when, in fact, the doctrine has been historically used to determine whether a breach occurred in the first instance.[54]

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49. Scalia notes that the unmistakability doctrine should be used to rebut the presumption that the government made no promise that one of its future sovereign acts would "incidentally disable it or the other party from performing one of the promised acts." *Id.* at 2477. As discussed *infra*, however, this a narrow reading of the scope of the unmistakability doctrine, which ignores the doctrine's importance in the determination of existing property rights under quasi-regulatory contracts. *See infra* notes 175–94 and accompanying text.

50. *Winstar*, 116 S. Ct. at 2478. Scalia also rejects the government's reserved powers doctrine based on the same reasoning in the majority opinion that the thrifts were not seeking to stay the exercise of sovereign authority. *Id.* The potential inconsistency between this reasoning and Justice Scalia's earlier rejection of the majority's remedy test in regards to the unmistakability doctrine may be explained in part by the strong precedent holding that the purpose of the reserved powers doctrine is to prevent the alienation of sovereign powers. *See, e.g.*, Stone v. Mississippi, 101 U.S. 814, 819 (1879) (no legislature can bargain away the public health or the public morals); *Winstar*, 116 S. Ct. at 2461 n.32. *See infra* note 154.

51. *Winstar*, 116 S. Ct. at 2482–84.

52. *Id.* at 2480.

53. *Id.* at 2480 (Rehnquist, J., dissenting) (citing United States v. Cherokee Nation of Okla., 480 U.S. 700, 707 (1987)); Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 51 (1986).

54. *Winstar*, 116 S. Ct. at 2481. Rehnquist does not elaborate on this fundamental criticism of the majority's opinion. *See infra* notes 155–59 and accompanying discussion for a more detailed critique. The dissent criticizes the majority's ruling (reached without applying the unmistakability doctrine) that the government assumed the risk for future regulatory change, characterizing the holding as a "finding of law" unsupported by judicial precedent. *Winstar*, 116 S. Ct. at 2482. In other words, Rehnquist is asserting that this finding is based upon the initial, legal conclusion that the unmistakability doctrine does *not* apply. (Rehnquist also criticizes Justice Breyer's characterization of the majority's allocation of risk holding as an "illusory factual finding.") *Id.* at 2485. Rehnquist also disagrees with Justice Scalia's similar conclusion (reached by *applying* the unmistakability doctrine) that the government made a binding promise not to change the regulatory treatment of the thrifts. Each of these findings are erroneous, according to the dissent, since they misconstrue both the applicability, and the substance of, the unmistakability doctrine. *Id.* at 2484–85.

The dissent also objects to the Court's limiting the sovereign acts doctrine to "public and general" acts which do not have "the substantial effect of releasing the government from its contractual obligations," an inquiry that necessarily involves the difficult question of whether the statute in question was "tainted by a governmental objective of self relief."[55] According to Rhenquist, the sovereign acts doctrine should be available as a defense to government liability for all "general regulatory enactments," regardless of their specific impacts upon private contractual rights.[56]

ANALYSIS OF THE *WINSTAR* DECISION

This section will analyze the *Winstar* decision, focusing in particular on the Court's treatment of the two main defenses raised by the government, the unmistakability and sovereign acts doctrines. These doctrines originated from two distinct government contractual models; one in which the government acts in a quasi-regulatory capacity and, in the other, as a market participant. Indeed, the problems with *Winstar* begin with the Court's attempt to address the government's sovereign defenses without distinguishing between these two very different models of government contracts. By ignoring this distinction, the Court misses its opportunity to craft a coherent framework in which rights under federal contracts may be addressed. Instead, the Court's separate opinions leave gaping holes in the law of federal contract interpretation while simultaneously blurring the respective roles of the unmistakability and sovereign acts doctrines in resolving contract disputes. This section will argue that the Court's failure to acknowledge the different models of government agreements has led to a remedy test that is legally insupportable, and to general uncertainty regarding both the appropriate application of the two sovereign defenses and the proper interpretation of the "unmistakability" standard. In particular, the limitations placed on the unmistakability doctrine by *Winstar* carry enormous potential consequences for the government's ability to regulate its contractual partners without violating the takings prohibitions of the Fifth Amendment. The effect of this judicial shift eliminating the presumption of reserved sovereign power over quasi-regulatory contractual rights will be discussed in a later section.

1. *Background on Sovereign Defenses and Government Agreements*

The first part of this section will discuss the background of the unmistakability and sovereign acts doctrines, and the distinction between

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55. *Winstar*, 116 S. Ct. at 2483.

56. *Id. See infra* notes 344-54 and accompanying text for an evaluation of *Winstar*'s "substantial effect" test.

"quasi-regulatory" and "market participant" agreements. This part will conclude with a brief presentation of the relationship between the two doctrines as applied to the different government contractual models.

a. Unmistakability Doctrine

The origin of the unmistakability doctrine can be traced back to 19th century federal cases in which courts grappled with the state's authority to abrogate existing contractual obligations entered into by previous state legislatures. Under the Contract Clause,[57] states were prohibited from eliminating vested rights arising out of public contracts.[58] Over time, however, courts adopted rules to minimize the effect of the Contract Clause on the exercise of state sovereign power. The first line of cases, which established what became known as the "reserved powers doctrine," held that the state could not contract away essential attributes of sovereignty such as the eminent domain or police power.[59] Under the reserved powers doctrine, state government contracts contain an implied reservation of the state's authority to exercise such "essential" powers in the future.[60] Because each contract incorporates the reservation into its terms, the state's subsequent exercise of its reserved powers does not violate the contract clause.[61] The contract clause cases did not, however, consider every aspect of the state's sovereign authority to be inalienable. A second line of decisions held that certain "non-essential" attributes of sovereignty, such as the state's taxing or spending powers,[62] could be contracted away,

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

58. *See* Fletcher v. Peck, 10 U.S. (6 Cranch) 87, 137 (1810). *See* Michael L. Zigler, *Takings Law and the Contract Clause: A Takings Law Approach to Legislative Modifications of Public Contracts*, 36 STAN. L. REV. 1447, 1449-51 (1984).

59. *See e.g,* West River Bridge Co. v. Dix., 47 U.S. (6 How.) 507 (1848) (state may not contract away the power of eminent domain); *Stone v. Mississippi*, 101 U.S. at 817-18; (no legislature can curtail the power of its successors to make such laws as they may deem proper in matters of police); *see also* Manigault v. Springs, 199 U.S. 473, 480 (1905); Home Bldg. & Loan Ass'n. v. Blaisdell, 290 U.S. 398, 434-435 (1934); Veix v. Sixth Ward Bldg. Ass'n, 310 U.S. 32, 38-39 (1940).

60. *Home Bldg. & Loan Ass'n*, at 435-36; *Veix*, at 38-39.

61. *Home Bldg. & Loan Ass'n*, at 430, 435 (reservation of essential attributes of sovereign power is incorporated in contracts as a postulate of the legal order). In United States Trust Co. v. New Jersey, 431 U.S. 1, 23-24 (1977), the Supreme Court reaffirmed that a state legislative action pursuant to its reserved powers does not violate the contract clause.

62. *United States Trust*, 431 U.S. at 24 (state may bind itself in the future exercise of the taxing and spending powers). In *Stone v. Mississippi*, 101 U.S. at 820, the Court observed:

> While taxation is in general necessary for the support of government, it is not part of the government itself. Government was not organized for the purposes of taxation, but taxation may be necessary for the purposes of government. As such, taxation becomes an incident to the exercise of the

providing the waiver of authority "had been specifically surrendered in terms which admit of no other reasonable interpretation."[63] This requirement that such "non-reserved" powers could be surrendered pursuant to express contractual language most closely resembles the unmistakability doctrine as it was subsequently interpreted by the Supreme Court.[64]

The forerunner to the unmistakability doctrine as applied to federal government contracts is the *Sinking-Fund Cases*.[65] In this early decision, the Supreme Court held that Congress' amendment of the terms of federal subsidy bonds, which required a private railroad to deposit money into a sinking fund to pay off its obligations to the government as they came due, did not deprive the railroad of due process or improperly interfere with any vested rights.[66] The Court based its holding on the language of the underlying statute issuing the bonds, which reserved Congress' right to subsequently "alter, amend and repeal [the] act."[67] In light of this statutory language, the Court found that the railroads did not possess contractual rights that superseded Congress' reserved power of amendment.[68]

> legitimate functions of government, but nothing more. No government dependent on taxation for support can bargain away its whole power of taxation...[but for] a consideration [the government] may, in the exercise of a reasonable discretion, and for the public good, surrender a part of its powers in this particular.

63. St. Louis v. United Ry. Co., 210 U.S. 266, 280 (1908). *See also* Keefe v. Clark, 322 U.S. 393, 396-97 (1944) ("obligation alleged to have been impaired must be clearly and unequivocally expressed."); Dodge v. Bd. of Educ., 302 U.S. 74, 78-79 (1937) (presumption is that state government has not conferred vested contractual rights to private parties); Jefferson Branch Bank v. Skelly, 66 U.S. (1 Black) 436, 446 (1861) (neither right of taxation nor any other power of sovereignty will be held to have been surrendered "unless such surrender has been expressed in terms too plain to be mistaken"); Charles River Bridge v. Warren Bridge, 36 U.S. (11 Pet.) 420, 548 (1837) ("continued existence of a government would be of no great value, if, by implications and presumptions, it was disarmed of the powers necessary to accomplish the ends of its creation").

64. *See Winstar*, 116 S. Ct. at 2455, n.21; Toscano, *supra* note 9, at 453, n.133.

65. Union Pac. R.R. Co. v. United States, 99 U.S. 700 (1878).

66. *See id.* at 719. The Court noted that the contract clause of the Constitution preventing the states from impairing the obligation of contracts was not applicable to the federal government. Nevertheless, the Court observed that the federal government (as well as the states) was still limited by the due process clause of the Constitution from impairing vested rights acquired through contract. *Id.* at 719-20.

67. *Id.* at 720. The Court characterized this language as indicating that "Congress not only retains, but has given special notice of its intention to retain, full and complete power to make such alterations and amendments of the charter as come within the just scope of legislative power." *Id.*

68. *Id.* at 719-20. The Court noted that "it is unnecessary to decide what power Congress would have had over the charter if the right of amendment had not been reserved; for, as we think, that reservation has been made." *Id.* at 719. Subsequent cases have held that Congress's reservation of sovereign authority exists even in the absence of express statutory language. *See, e.g.*, Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 808 (9th Cir. 1990);

The unmistakability doctrine was not officially enunciated by the Supreme Court until over 100 years later, in *Merrion v. Jicarilla Apache Tribe.*[69] In *Merrion,* private development interests entered into oil and gas leases with an Indian tribe, which granted free access to explore for and develop resources in exchange for an up-front cash bonus, royalties and rents.[70] When the tribe taxed the lessees' activities, the lessees brought suit alleging, among other claims, that the imposed taxes violated the terms of the underlying leases.[71] The Supreme Court disagreed, holding that the tribe did not waive its sovereign authority merely because it failed to reserve the express right to exercise such authority in a commercial agreement.[72] Instead, the Court observed that sovereign power "is an enduring presence that governs all contracts subject to the sovereign's jurisdiction, and will remain intact unless surrendered in unmistakable terms."[73]

Following *Merrion,* the Court decided *National Railroad Passenger Corp. v. Atchison Topeka Santa Fe Railway Co.*[74] In *National Railroad,* private railroad companies claimed that the government had "impaired" statutorily-based contracts by subsequently amending the statute (and consequently the underlying contracts) to require the railroads to pay a 25% reimbursement to Amtrak for providing free rail service to railroad employees.[75] Without specifically addressing the unmistakability doctrine,

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Democratic Cent. Comm. v. Washington Metro. Area Transit Comm., 38 F.3d 603, 607 (D.C. Cir. 1994); Great Lakes Higher Educ. Corp. v. Cavazos, 911 F.2d 10, 16 (7th Cir. 1990); Educational Assistance Corp. v. Cavazos, 902 F.2d 617, 629, n.20 (8th Cir. 1990); Ohio Student Loan Comm'n v. Cavazos, 900 F.2d 894, 901-902 (6th Cir. 1990); South Carolina State Educ. Assistance Auth. v. Cavazos, 897 F.2d 1272, 1275-76 (4th Cir. 1990).

69. *See* Merrion v. Jicarilla Apache Tribe, 455 U.S. 130 (1982). In the meantime the Court had made two important decisions regarding property right acquired under government contracts. In the first, Lynch v. United States, 292 U.S. 571, 577-79 (1934), the Court held that Congress' repeal of its obligations to pay benefits under a federally operated insurance plan violated the Fifth Amendment's takings prohibition. In the second, Perry v. United States, 294 U.S. 330, 349-54 (1935), the Court found the government's refusal to pay bondholders in gold according to the terms of the notes violated the bond holders' contractual rights. *Perry* and *Lynch* are routinely cited for the proposition that the government should be treated as any other private party in the interpretation of federal contract rights. *See, e.g., Winstar,* 116 S. Ct. at 2473 (Breyer's concurrence). However, neither of these decisions address the government's sovereign defenses as embodied by the ummistakability and sovereign acts doctrines. For a discussion of how *Perry* and *Lynch* may be interpreted in the context of the quasi-regulatory and market participant models of government contracts, see *infra* notes 355-63 and accompanying discussion.

70. *Merrion* 455 U.S. at 135.

71. *Id.* at 148.

72. *Id.*

73. *Id.*

74. National R.R. Passenger Corp. v. Atchison Topeka Santa Fe Ry. Co., 470 U.S. 451 (1985).

75. *Id.* at 465, 477.

the Court rejected the railroads' claims that the statute had conferred vested contractual rights, holding that:

> [A]bsent some clear indication that the legislature intends to bind itself contractually, the presumption is that 'a law is not intended to create private contractual or vested rights but merely declares a policy to be pursued until the Legislature shall ordain otherwise.'[76]

After examining the statute and finding reservation language similar to the reservation in *Sinking-Fund Cases*, the Court concluded "[t]his is hardly the language of contract."[77]

The Court returned to the unmistakability doctrine in *Bowen v. Public Agencies Opposed to Social Security Entrapment*.[78] Under section 418 of the to the Social Security Act of 1935,[79] state agencies could participate in the social security system pursuant to agreements entered into between the state and the federal government. Section 418(g) allowed states to withdraw their employees from coverage upon two years notice. In response to the threat of increasing withdrawals of state employees throughout the nation, however, Congress amended section 418(g) in 1983 to eliminate the states' right of withdrawal. The State of California and several of its agencies thereupon sued, alleging several claims that were ultimately consolidated before the Supreme court as an action against the United States for an unconstitutional taking of property.[80] The Supreme Court rejected the state's

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76. *Id.* at 465–66 (quoting Dodge v. Bd. of Educ., 302 U.S. 74, 79 (1937)). The notion that government contracts contain an implied "presumption" that the government is not waiving its right to exercise sovereign powers was adopted by Justice Scalia in *Winstar*. *Winstar*, 116 S. Ct. at 2477 (Scalia, J., concurring).

77. *National R.R.*, 470 U.S. at 467. In determining whether a statute gives rise to a contractual obligation, the Court noted, "it is of first importance to examine the language of the statute." *Id.* at 466 (citing *Dodge v. Board of Education*, 302 U.S. at 78; *see generally* Indiana *ex. rel.* Anderson v. Brand, 303 U.S. 95, 104 (1938)). After finding that the statute conferred no vested contractual rights, the Court examined the individual agreements, which it characterized as valid contracts between the private railroads and the private railroad company Amtrak. Applying the less rigorous review standard appropriate to the Fifth Amendment's due process guarantee, *National R.R.*, 470 U.S. at 472–73 n.25 (citing Pension Benefit Guar. Corp., 467 U.S. 717, 732–733 (1984)), the Court found that the amendments had not impaired any private contractual rights. *National R.R.*, 470 U.S. at 478.

78. *Bowen*, 477 U.S. 41.

79. 42 U.S.C §§ 1301–14301.

80. The agencies claimed that their "property rights" had been taken without just compensation in violation of the Fifth Amendment. In a separate lawsuit, the State sought to enjoin Congress' amendment which eliminated the withdrawal provisions as well as a declaration that the amendment was unconstitutional. These lawsuits were consolidated before the district court, which held that the withdrawal provision created a constitutionally protected property right whose elimination without just compensation violated the Fifth Amendment. The district court found that the "only rational compensation" would be

claim, holding that "contractual arrangements, including those to which a sovereign itself is party, 'remain subject to subsequent legislation' by the sovereign."[81] The Court noted that Congress had reserved the right "to alter, amend, or repeal any provision" of the Social Security Act[82] and that each state agreement had been executed in accordance with this reservation.[83] The Court went on to characterize the termination provision:

> The termination clause was not unique to this Agreement; nor was it a term over which the State had any bargaining power or for which the State provided independent consideration. Rather, the provision simply was part of a regulatory program over which Congress retained authority to amend in the exercise of its power to provide for the general welfare.[84]

The Court concluded by holding that, since the section 418 agreement had incorporated the government's power to amend or alter certain provisions of the agreement, the state had no property right in the repealed withdrawal provision and thus no takings had occurred.[85]

The unmistakability doctrine was again revisited in *United States v. Cherokee Nation of Oklahoma*.[86] *Cherokee Nation* concerned a treaty agreement

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reimbursement to the State or public agencies of the amount of money they were paying to the United States to participate in the Social Security Program. Finding that these "just compensation" damages would be "clearly contrary to the will of Congress" in attempting to solve the financial crises of the Social Security System, the district court ruled the amendment to be unconstitutional. *Bowen*, 477 U.S. at 51; *see also* Public Agencies Opposed to Soc. Sec. Entrapment v. Heckler, 613 F. Supp. 558, 575 (E.D. Cal. 1985). In *Winstar*, Justice Souter seizes on the district court's reasoning to carve out an exception to the remedy test, in which the unmistakability doctrine would be applicable to claims for money damages whenever such claims would be "the equivalent of exemption from the terms of the subsequent statute," as was the case in *Bowen*. *See Winstar*, 116 S. Ct. at 2457. This approach may be critiqued on two grounds. First, the approach was not adopted by the Supreme Court's own reasoning in *Bowen*. Second, the approach makes an essentially superficial distinction in quasi-regulatory takings cases between government regulations that directly impose costs on a private party (the imposition of a tax or the increase in a royalty rate for example) versus regulations that reduce the value of the alleged property right by means other than increased payments to the government. *See infra* notes 160–68 and accompanying text.

81. *Bowen*, 477 U.S. at 52, *quoting* Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 147 (1982).

82. *Bowen*, 477 U.S. at 51, n.18; *see* 42 U.S.C. § 1304 (1994).

83. *Bowen*, 477 U.S. at 54. The agreement provided that its terms "were in conformity with § 418." *Id.*

84. *Id.* at 55. The Court thus distinguished its decision from Lynch v. United States, 292 U.S. 571 (1934), on the basis that unlike the plaintiffs in *Lynch*, the state had not paid a monetary premium for the "right" eliminated by the Congressional statute. *Bowen*, 477 U.S. at 55.

85. *Id.* at 55–56.

86. United States v. Cherokee Nation of Okla., 480 U.S. 700 (1987).

in which the federal government had conveyed property rights in a riverbed to an Indian tribe. When the federal government began making navigational improvements to the river, the tribe sued, claiming just compensation damages for a Fifth Amendment taking of property.[87] The Supreme Court held that no taking had occurred since the treaty remained subject to the federal government's navigational easement, a sovereign power that had not been conveyed by the treaty.[88]

Before turning to an examination of the sovereign acts doctrine, it is worthwhile to note two important aspects of the Supreme Court's unmistakability doctrine decisions. First, the Court's decisions borrow heavily from the contract clause cases in formulating the parameters under which the federal government may surrender sovereign power, without ever describing the relationship between federal unmistakability and state contract clause law. Keeping in mind the settled law that the prohibitions of the contract clause are not applicable to the federal government,[89] the degree to which the unmistakability doctrine adopts the standards and reasoning underlying the contract clause nevertheless remains uncertain.[90] In contrast to the contract clause cases, for example, the unmistakability decisions make no distinction between reserved (and therefore inalienable) and non-reserved sovereign powers.[91] As discussed above, the lineage of the unmistakability doctrine can be traced back to contract clause decisions involving the permissible waiver of non-reserved powers such as taxing or spending.[92] While *Sinking Fund Cases, Merrion, National Railroad,* and *Cherokee Nation* each arguably involve the alleged waiver of such non-reserved powers, the Court does not rely on this fact in applying the unmistakability doctrine. Instead, these decisions describe federal sovereignty only in general terms, relying on cases involving both reserved and non-re-

87. *Cherokee Nation,* 480 U.S. at 702.

88. *Cherokee Nation,* 480 U.S. at 706. *Winstar* distinguishes *Cherokee Nation* by finding that "an order to pay compensation would have placed the Government in the same position as if the navigational easement had been surrendered altogether." *Winstar,* 116 S. Ct. at 2457 n.23. *See infra* notes 160–68 and accompanying discussion.

89. Pension Guar. Corp. v . R. A. Gray & Co., 467 U.S. 717, 733 (1983); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 719 (1878).

90. Justice Souter notes that the "want of more developed law on limitations independent of the Contract Clause is in part the result of applying the unmistakability canon of construction to avoid this doctrinal thicket . . . " *Winstar,* 116 S. Ct. at 2455.

91. *See infra* notes 150–56 and accompanying text.

92. *See supra* note 63 and accompanying text. *See also* United States Trust Co. v. New Jersey, 431 U.S. 1, 24 (1977) (state may bind itself in the future exercise of the taxing and spending powers); Stone v. Mississippi, 101 U.S. 814, 820 (1879) (taxation is incidental to the essential sovereign powers of government).

served powers.[93] Moreover, in *Bowen* the Court applied the unmistakability doctrine to Congress' administration of the social security system, an authority similar to the traditionally inalienable police power held by the states.[94] Numerous federal cases have followed *Bowen*'s example and applied the unmistakability doctrine to the alleged contractual waiver of various "police-like" sovereign powers.[95] Finally, in *Winstar*, Justice Souter considers the application of the unmistakability doctrine to FIRREA, despite his conclusion that the power to regulate thrifts is "within the police

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93. In *Merrion*, for example, the Court cites from state contract clause cases involving the alleged surrender of the police power (a reserved, inalienable power) Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 147–48 (1982) (citing Veix v. Sixth Ward Bldg. & Loan Ass'n, 310 U.S. 32 (1940); Home Bldg. & Loan Ass'n. v. Blaisdell, 290 U.S. 398 (1934)) and the taxing power, a non-reserved power that may be surrendered pursuant to express contractual language. *Jicarilla Apache*, 455 U.S. at 148 (citing St. Louis v. United Rys. Co., 210 U.S. 266, 280 (1908)).

94. *See, e.g., Stone*, 101 U.S. at 818 (inalienable police power extends to all matters affecting the public health or morals). *Blaisdell*, 290 U.S. at 435–36; *Veix*, 310 U.S. at 38–39. An argument can be made that the social security system is more akin to a taxing program than an exercise of the police power. *See, e.g.*, Helvering v. Davis, 301 U.S. 619, 645–46 (1936). This point ignores the fact that the states originally had the option of joining the system (as of this writing not all states participate) and thus their payments can be better characterized as voluntary participation in a regulatory program. The argument also ignores the overall public purpose of the social security system to establish an insurance program for "persons working in industry and commerce as a long-run safeguard against the occurrence of old-age dependency." Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 43 (1986) (citing H.R. Rep. No. 81-1300, at 3 (1949)).

95. *See, e.g.*, Water contract cases: O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995) (unmistakability doctrine applied to modification of water contracts due to passage of statute intended to restore ecological integrity to the Delta); Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 812–13 (9th Cir. 1990) (court applies unmistakability doctrine to amendments to Reclamation Act that limit volume of subsidized water to leased lands in order to promote family farming in western states). Mineral Leasing Cases: Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780, 789 (D.C. Cir. 1990) (court applies unmistakability doctrine to amendments to Mineral Lands Leasing Act altering terms under which government allows access to coal reserves on public lands); Western Energy Co. v. Dep't of Interior, 932 F.2d 807 (9th Cir. 1991); Trapper Mining Inc. v. Lujan, 923 F.2d 774 (10th Cir. 1991); Coastal States Energy Co. v. Hodel, 816 F.2d 502 (10th Cir. 1987); FMC Wyoming Corp. v. Hodel, 816 F.2d 496 (10th Cir. 1987); Student Loan Cases: Association of Accredited Cosmetology v. Alexander, 979 F.2d 859, 867 (D.C. Cir. 1992); (court applies unmistakability doctrine to congressional amendments altering terms of the federal student loan program); Rhode Island Higher Educ. Assistance Auth. v. Secretary, United States Dep't of Educ., 929 F.2d 844, 850-51 (1st Cir. 1991); Great Lakes Higher Educ. Corp. v. Cavazos, 911 F.2d 10, 16 (7th Cir. 1990); Educational Assistance Corp. v. Cavazos, 902 F.2d 617, 629, n.20 (8th Cir. 1990); Ohio Student Loan Comm'n v. Cavazos, 900 F.2d 894, 901-902 (6th Cir. 1990); South Carolina State Educ. Assistance Auth. v. Cavazos, 897 F.2d 1272, 1275-76 (4th Cir. 1990).

power."[96] This article will return to this aspect of unmistakability doctrine law in the next section. Here it is sufficient to note the tension between the application of the unmistakability doctrine to the sovereign's continued exercise of reserved, *inalienable* powers and Justice Souter's argument that the sole purpose of the doctrine is to prevent the implied surrender of such powers.[97]

A second important aspect of the unmistakability cases is how they illustrate the essentially interpretive role of the unmistakability doctrine in determining the rights and duties of the federal and private parties to quasi-regulatory agreements. In each case, a party claimed a "property right," arising under the agreement, which was allegedly harmed by an act of the sovereign's authority. In each case, the Court found that, given the absence of unmistakable language to the contrary, the contractual right was subject to the continuing exercise of sovereign authority and thus the government owed no duty of compensation for the impairment of the alleged property right. This article will discuss this aspect of the unmistakability doctrine (as an interpretive tool to determine property rights under quasi-regulatory agreements) in more detail in later sections.[98]

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96. *Winstar*, 116 S. Ct. at 2462, n.34 (citing *Veix*, 310 U.S. at 38). In fact, *Winstar*, *Bowen* and the many cases cited *supra*, note 94, illustrate the difficulty in distinguishing between reserved and non-reserved powers at the federal level where taxing, spending and general regulatory powers are often intricately intertwined.

97. *See infra*, notes 150–56 and accompanying text. In other words, the application of the unmistakability doctrine (which allows for the surrender of sovereign power pursuant to express language) to inalienable, reserved powers only makes sense if the doctrine is interpreted to limit the government's implied assumption of contractual liability for the exercise of such powers. The tension described above assumes, of course, that certain federal sovereign powers akin to the police power are reserved and therefore inalienable. Clearly one can make the common sense argument that the principle underlying the reserved powers doctrine,—that essential sovereign powers must always be retained to allow the functioning of government—applies with even greater force to the important regulatory responsibilities of the federal government. While no court has directly addressed this issue, *see* Toscano, *supra* note 9, at 460, several have cited *Bowen* for the authority that the federal police power may be contracted away under the unmistakability doctrine. *See, e.g.*, Far West Fed. Bank v. Director, Office of Thrift Supervision, 738 F. Supp. 1564, 1570 (D. Or. 1990), *rev'd*, 951 F.2d 1093 (9th Cir. 1991) (federal government can waive its police power in a contract if it does so clearly and unmistakably); Century Federal Sav. Bank v. United States, 745 F. Supp. 1363, 1369 (N.D. Ill. 1990) (federal government may waive its police power in some circumstances). For an interpretation of the unmistakability doctrine which preserves the federal reserved power, *see infra*, notes 149–54 and accompanying text. In response to the government's arguments that the reserved powers doctrine should apply equally to federal government contracts, Justice Souter notes simply, "[t]his may be so but is also beside the point . . . ." *Winstar*, 116 S. Ct. at 2461.

98. *See infra* notes 143–44 and 245–47 and accompanying text.

b. Sovereign Acts Doctrine

The sovereign acts doctrine was first enunciated by the claims court in *Deming v. United States.*[99] In *Deming,* the government had entered into a fixed-price contract to supply rations to the Marine Corps. Before the contract was performed, Congress passed the Legal Tender Act, which significantly raised the cost of the rations to be furnished.[100] The claims court rejected the plaintiff's claim that the government had breached the contract by imposing new terms based on the following reasoning:

> [The fallacy of the plaintiff's claim is] that it supposes general enactments of Congress are to be construed as evasions of [the plaintiff's] particular contract. This is a grave error. A contract between the government and a private party cannot be *specially* affected by the enactment of a *general* law . . . . [T]he government entering into a contract, stands not in the attitude of the government exercising its sovereign power of providing laws for the welfare of the State. The United States as a contractor are not responsible for the United States as a lawgiver. Were this action brought against a private citizen . . . it could not possibly be sustained. In this court the United States can be held to no greater liability than other contractors in other courts.[101]

Almost immediately following *Deming,* the claims court applied the sovereign acts doctrine in *Jones v. United States.*[102] In *Jones,* civil engineers incurred additional expenses in performing government survey contracts due to the government's withdrawal of military protection in Indian territory during the 1850s. As in *Deming,* the court rejected the plaintiffs' breach of contract claims by holding that the United States could not be held liable in its contractual capacity for its actions taken as a sovereign.[103] Such actions, noted the court, "so long as they be public and general, cannot be deemed to specially alter, modify, obstruct or violate the particular contracts into which [the government] enters with private persons."[104]

The sovereign acts doctrine was adopted by the Supreme Court in *Horowitz v. United States.*[105] In *Horowitz* the government had entered into a supply contract with Horowitz for the purchase of silk. Due to a subsequent embargo placed upon silk shipments by the Railroad Administration, the

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99. Deming v. United States, 1 Ct. Cl. 190 (1865).
100. *Id.*
101. *Id.* at 191 (emphasis in original).
102. Jones v. United States, 1 Ct. Cl. 383 (1865).
103. *Id.* at 384.
104. *Id. See also* Wilson v. United States, 11 Ct. Cl. 513, 521 (1875).
105. Horowitz v. United States, 267 U.S. 458, 461 (1925).

government was unable to perform timely delivery of the silk. As a result of falling silk prices, the delay caused damages to Horowitz , who thereupon sued the government for breach of contract.[106] The Supreme Court agreed that the government had failed to perform its contractual obligation but held that the government's breach was excused by the embargo, which the Court characterized as a "public and general" act enacted by the government in its sovereign capacity.[107]

The key to understanding the sovereign acts doctrine lies in its essential purpose, to treat the government as any other private party in determining liability for unexpected sovereign acts that hinder or block contractual performance. A basic principle of contract law is that a contracting party will be held responsible for damages caused by its own actions. Thus, the sovereign acts doctrine asks whether the government action impeding performance can be fairly attributed to the government in its role as contractor.[108] In *Winstar*, Justice Souter found that government actions, even though general in nature and enacted in a sovereign capacity, will be attributable to the government as contractor whenever such actions have "the substantial effect of releasing the Government from its contractual obligations. . . ."[109] If the sovereign act is not attributable to the government as contractor, the government must still show that it would not be liable under "ordinary principles of contract law."[110] In *Winstar*, the government raised the sovereign acts doctrine as an excuse for its failure to perform on its promise to provide favorable regulatory treatment. Thus, the government was required to meet the common law standards of commercial impossibility,[111] which include a finding that the sovereign act

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106. *Id.* at 460.

107. *Id.* at 461. The Court relied specifically on *Deming* and *Jones* to reach its holding. Deming v. United States, 1 Ct. Cl. 190 (1865); *Jones*, 1 Cl. Ct. 383.

108. *See* Richard E. Speidel, *Implied Duties of Cooperation and the Defense of Sovereign Acts in Government Contracts*, 51 GEO. L.J. 516 (1963). Professor Speidel notes, "[t]he apparent result of this doctrine of 'dual capacity' is that the United States as a contractor has an implied duty of cooperation, but the United States as a 'sovereign' does not." *Id.* at 518.

109. *Winstar*, 116 S. Ct. at 2467. This holding of *Winstar*, which narrows the "public and general act" standard of *Horowitz*, will be discussed *infra*, notes 339-50.

110. *Id.* at 2465.

111. *Winstar*, 116 S. Ct. at 2469. In this instance, the sovereign acts doctrine allows the government the same right as any other private party to have its contractual non-performance excused through commercial impossibility due to some act of the federal government. Note that the *Winstar* scenario, in which the government must successfully meet the impossibility standards, arises only in situations where the sovereign action has prevented the *government* from performing on a contractual promise. Sovereign acts may also hinder the performance of private parties as well. *See e.g.*, Tony Downs Foods Co. v. United States, 530 F.2d 367, 372 (Cl. Ct. 1976) (poultry supplier to Department of Agriculture forced to incur losses as a result of government's termination of the national price freeze for certain products); *Deming*, 1 Cl. Ct. at 190 (government food supplier forced to incur

was an event contrary to the basic assumptions on which the parties contractually agreed and that the language or circumstances surrounding the agreement do not indicate otherwise.[112]

c. *Sovereign Defenses and Models of Government Contractual Agreements*

A review of the above-cited cases reveals that prior to their convergence in *Winstar*, the unmistakability and sovereign acts doctrines had never been addressed by the Supreme Court in the same case. This doctrinal separation is attributable only in part to the different historical lineages, as described above, of the two doctrines. Upon closer examination one sees that 1) the doctrines have been applied to two contrasting models of government contractual agreements; and 2) the Court's reasoning in applying the two doctrines to their respective contractual models has been fundamentally different.

The contractual model in which the Court has considered the unmistakability doctrine might best be described as "quasi-regulatory." Under this model, the government offers private parties the chance to enter into contractual arrangements as part of a greater regulatory program, while still retaining (either expressly or by implication) the authority to amend such arrangements in the exercise of its power to provide for the general welfare.[113] Such contractual arrangements may range from supplying water to arid areas in the west,[114] permitting access to resources on federal property,[115] insuring state student loan programs,[116] or establishing

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additional expenses as a result of Congressional passage of Legal Tender Act); *Jones*, 1 Cl. Ct. at 384 (civil engineers required to incur additional expenses as a result of government withdrawal of military support to protect surveying crews).

112. *Winstar*, 116 S. Ct. at 2469-72. These requirements were adopted from the language of the RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981), stated *supra* note 39.

113. *Bowen*, 477 U.S. at 55. While some decisions have characterized quasi-regulatory agreements as non-contractual in nature, *see infra* note 202, this article will treat such agreements as contracts, which confer valuable, though qualified, rights on private parties.

114. *See* O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995); Madera Irrig. Dist. v. Hancock, 985 F.2d 1397, 1404, 1406-07 (9th Cir. 1993); Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 811-12 (9th Cir. 1990).

115. *See* Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780, 789 (D.C. Cir. 1990); *see also* Western Energy Co. v. Dep't of Interior, 932 F.2d 807 (9th Cir. 1991); Trapper Mining Inc. v. Lujan, 923 F.2d 774 (10th Cir. 1991); Coastal States Energy Co. v. Hodel, 816 F.2d 502 (10th Cir. 1987); FMC Wyoming Corp. v. Hodel, 816 F.2d 496 (10th Cir. 1987).

116. *See* Association of Accredited Cosmetology v. Alexander, 979 F.2d 859, 867 (D.C. Cir. 1992); Rhode Island Higher Educ. Assistance Auth. v. Secretary United States Dep't of Educ., 929 F.2d 844, 850-51 (1st Cir. 1991); Great Lakes Higher Educ. Corp. v. Cavazos, 911 F.2d 10, 16 (7th Cir. 1990); Educational Assistance Corp. v. Cavazos, 902 F.2d 617, 629, n.20 (8th Cir. 1990); Ohio Student Loan Comm'n v. Cavazos, 900 F.2d 894, 901-902 (6th Cir. 1990); South Carolina State Educ. Assistance Auth. v. Cavazos, 897 F.2d 1272, 1275-76 (4th Cir. 1990).

a framework in which private parties may profitably satisfy the nation's needs for low income housing.[117] Quasi-regulatory agreements do not generally involve the arms-length bargaining and negotiation typical of more standard contractual arrangements. Instead, the government usually offers an option for private parties to participate in the government's program according to statutes and regulations with pre-established guidelines for exchanges of consideration and terms of dealing.[118] Despite the lack of bargained-for consideration, agreements entered into under the quasi-regulatory model generally confer valid rights, which may be qualified, however, by the government's exercise of sovereign regulatory authority.[119]

In contrast, cases in which the sovereign acts doctrine has historically been raised involve contractual agreements in which the government acts in the role of market participant.[120] Typical agreements under this model involve routine supply or service contracts, which the government enters into in order to keep its own operations running smoothly.[121] The sovereign acts doctrine fits well with the market participant model by treating the government as a private party, with the

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117. Cisneros v. Alpine Ridge Group, 508 U.S. 10 (1993); F.H.A. v. Darlington, Inc., 358 U.S. 84 (1958); Parkridge Investors Ltd. Partnership v. Farmers Home Admin., 13 F.3d 1192 (8th Cir. 1994); Housing Auth. of Fort Collins v. United States, 980 F.2d 624 (10th Cir. 1992); Lifgren v. Yeuter, 767 F. Supp. 1473 (D. Minn. 1991).

118. The exchange of consideration may thus distinguish quasi-regulatory agreements from programs in which the recipients provide no consideration for receiving government benefits. *See, e.g.*, Bowen v. Gilliard, 483 U.S. 586, 604-05 (1987) (families receiving AFDC payments have no protected property rights to continued benefits at same level).

119. As discussed *infra*, courts generally characterize such qualified contractual rights as something less than "property" as defined by the contours of the Fifth Amendment. *See, e.g., Bowen*, 477 U.S. at 51-52 (contractual right at issue bears little resemblance to rights held to constitute property within meaning of Fifth Amendment); *Darlington, Inc.*, 358 U.S. at 90 (rights are ones that lie in the periphery where vested rights do not attach); Mitchell Arms, Inc. v. United States, 7 F. 3d 212, 217 (Fed. Cir. 1993) (enforceable rights sufficient to support a takings claim cannot arise in an area voluntarily entered into and one which is subject to pervasive government control). *See infra* notes 203-30 and accompanying discussion regarding nature of property rights conferred by agreements falling within the quasi-regulatory model.

120. For a more detailed description of the government's role as market participant see Joseph Sax, *Takings and the Police Power*, 74 YALE L.J. 36, 62-63 (1964). *See also* Joshua Schwartz, *Liability for Sovereign Acts: Congruence and Exceptionalism in Government Contracts Law*, 64 GEO. WASH. L. REV. 633 (1996); Janice C. Griffith, *Local Government Contracts: Escaping from the Governmental/Proprietary Maze*, 75 IOWA L. REV. 277 (1990).

121. These are the contracts described by Justice Souter in *Winstar* as "humdrum supply contracts," which "no one would seriously contend" might be subject to the unmistakability doctrine. 116 S. Ct. at 2457.

same liabilities and contractual rights that a private party would have in the face of sovereign acts which hinder or bar contractual performance.[122]

Clearly not all government contracts fall readily into either the "quasi-regulatory" or "market participant" model. This article will return to the sometimes difficult question of how a court might differentiate between the two models of government contracts in the last section. The next part of this section will illustrate how these different contractual models have influenced the courts' treatment of the unmistakability and sovereign acts doctrines in interpreting government contract disputes.

d. Relationship Between the Unmistakability and Sovereign Acts Doctrines as Applied to Government Contractual Agreements

The unmistakability and sovereign acts doctrines both act to minimize the constraints on the government's freedom to legislate that may arise as a result of the government's contractual commitments. Beyond this shared purpose, however, judicial precedent offers little guidance in delineating the interaction between the two doctrines. The last section of this article will propose a general comprehensive framework under which one may apply the doctrines to federal contract dispute resolution.[123] The purpose of this subsection is simply to present some basic points regarding the relationship between the doctrines, including their respective roles in interpreting rights under the two government contractual models described above.

The most fundamental distinction between the unmistakability and sovereign acts doctrines lies in their contrasting roles in resolving governmental contract disputes. The unmistakability doctrine is used by a court to determine the nature of the contractual obligation that has been created and to establish the respective rights of the parties to the underlying contract.[124] In making this determination, the unmistakability doctrine directs a court, absent unmistakable language to the contrary, to find for the continued retention of sovereign authority.[125] In contrast to the

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122. *See supra* notes 99–112 and accompanying text.

123. *See infra* notes 287–371 and accompanying text.

124. *See, e.g.*, Statesman Sav. Holding Corp. v. U.S., 26 Cl. Ct. 904, 920 (1992) (purpose animating the unmistakability doctrine makes it clear that the doctrine controls how contractual rights with the government are *created*). This determination may require an analysis of whether the contract terms surrender certain specific powers (such as the power of taxation or the navigational easement as was analyzed in *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130 (1982) or *United States v. Cherokee Nation*, 480 U.S. 700 (1997)), or instead, whether the contract terms surrender the more general power to change the regulatory structure in the future (as was analyzed in *Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment*, 477 U.S. 41, 43 (1986)).

125. *See supra* note 27.

unmistakability doctrine, the sovereign acts doctrine is not an interpretive tool, but instead a mechanism whereby the government may avoid liability in its contractual capacity for its actions taken as a sovereign. In evaluating the sovereign acts defense, a court will ask not whether the government has retained its sovereign powers (this is assumed), but instead whether the government, as market participant, should be held responsible under the terms of the contract for the exercise of such powers.

This essential difference comes more clearly into focus upon reviewing the cases interpreting the two doctrines. As stated in *Jones*, the sovereign acts doctrine stands for the proposition that public and general acts do not specifically alter, modify, obstruct, or violate the particular contracts entered into between the government and a private party.[126] Instead, the sovereign act is considered to be an event essentially beyond the control of the contracting parties. Under this framework, the government is treated as a private party, for whom liability will accrue according to how the contract (and contract law) allocates such unavoidable risks. If the government claims impossibility as a result of the sovereign act, the successful assertion of the defense will normally result in the discharge of each party's respective obligations to perform on the contract.[127]

Consider the difference between this scenario and the application of the unmistakability doctrine to the quasi-regulatory contracts as described above. Under the quasi-regulatory model, subsequent sovereign acts often modify the contractual agreements at issue, which are not discharged but instead remain in force, albeit with potentially amended terms.[128] The best example of this is *Bowen*, in which the Court upheld the Department of Health and Human Services' rejection of California's termination request based on the legislative modification which had altered the terms of the social security agreement by eliminating the statutory

126. Jones v. United States, 1 Cl. Ct. 383, 384 (1865). As discussed above, such contracts would typically fall under the market participant model, in which the government enters into the contract as a market participant rather than as a quasi-regulator.

127. RESTATEMENT (SECOND) OF CONTRACTS: DISCHARGE BY SUPERVENING IMPRACTICABILITY § 261 (1981). Where one party has already rendered partial performance, that party is entitled to recover restitution in a court of equity. RESTATEMENT (SECOND) OF CONTRACTS: RELIEF INCLUDING RESTITUTION § 272 (1981).

128. *See, e.g., Bowen v. Public Agencies*, 477 U.S. at 54-56; National R.R. Passenger Corp. v. Atchison Topeka Santa Fe Ry. Co., 470 U.S. 451, 467 (1985); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 718 (1878); *see also* Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780, 789 (D.C. Cir. 1990) and other Mineral Lands Leasing Act cases cited *supra* note 95; O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995); other water contract cases cited at note 95; Association of Accredited Cosmetology v. Alexander, 979 F.2d 859, 867 (D.C. Cir. 1992); other student loan cases cited *supra* note 95; Housing Auth. of Fort Collins v. United States, 980 F.2d 624, 630, 631 (10th Cir. 1992).

withdrawal option.[129] In *Bowen*, the Court used the unmistakability doctrine to establish the terms of an agreement, on which California was still obligated to perform by means of continued social security payments.[130]

In the quasi-regulatory model, the government is, quite appropriately, not treated as a private party, but instead as a sovereign authority, which has entered into a contractual arrangement in order to accomplish a regulatory purpose. There is no issue of whether the sovereign act is attributable to the government in its contracting capacity; clearly it is.[131] In contrast to the analysis under the sovereign acts doctrine, however, this convergence of governmental roles does not necessarily render the government liable for damages to the private party.[132] Instead, a court will examine the relationship between the contract in question and the statutory authority for the contract's creation in order to determine whether the terms of a subsequent sovereign act should be incorporated into the contractual agreement.[133] If the court finds a sufficient relationship between the organic statute and the sovereign act, the newly enacted terms may become part of the underlying contract, altering if necessary the contractual rights of the private party.[134]

Under the sovereign acts doctrine, a court's analysis will differ significantly. If the government's assertion of the doctrine is based on an impossibility defense,[135] a court will inquire into whether the sovereign "act" was an unforeseeable event from the viewpoint of the contracting parties.[136] In *Horowitz*, for example, the sovereign act found to excuse the government's obligation for timely shipment was an embargo by the Railroad Administration, a federal agency not involved in the shipment contract, acting pursuant to a statute that presumably had no relation to the statutory authority used by the government to enter into salvage contracts for silk.[137] The analysis required to raise the sovereign acts doctrine as a

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129. *Bowen v. Public Agencies*, 477 U.S. at 54–56.

130. *Id.* at 53–55. *See supra* notes 78–85 and accompanying text.

131. In other words, both the execution of the quasi-regulatory agreement and the subsequent legislative enactment are acts attributable to the government acting in a sovereign capacity.

132. For a different view see *infra* note 344 and accompanying text.

133. *See, e.g., Bowen*, 477 U.S. at 54–56. *See also National Railroad*, 470 U.S. at 467; cases cited *supra* note 94.

134. *Id.* See *infra* notes 307–12 and accompanying discussion regarding what constitutes a relationship between the underlying statute and the sovereign act that is sufficient to justify the incorporation of new contractual terms.

135. *See supra* notes 39, 111 and accompanying text.

136. *Winstar*, 116 S. Ct. at 2469, *citing* RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981) (was the sovereign act an event contrary to the assumptions of the parties at the time the contract was entered into?).

137. Horowitz v. United States, 267 U.S. 458, 459-60 (1925).

defense makes its successful assertion unlikely in a highly regulated field where the "sovereign act" alleged to excuse performance is a natural (and thus arguably foreseeable) consequence of the regulatory environment.[138] In contrast, when courts apply the unmistakability doctrine to interpret quasi-regulatory agreements, the likelihood of a future exercise of sovereign power typically strengthens the presumption that the government has reserved its authority to amend the terms of the contract.[139] As a result, quasi-regulatory agreements are even *more* likely to be subject to subsequent sovereign acts where the exercise of sovereign power is

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138. This fact was not lost on Justice Souter who nevertheless cautioned that "we do not say that [the conditions to satisfy the sovereign acts defense] can never be satisfied when the Government contracts with participants in a highly regulated industry for particular regulatory treatment." *Winstar*, 116 S. Ct. at 2469.

139. This result is supported, in part, by the role the unmistakability doctrine plays in determining property rights under quasi-regulatory agreements. In conducting such an analysis, courts will borrow from regulatory takings law, asking whether the government's amendment of the contractual terms has upset the "reasonable expectations" of the private contracting party. *See, e.g.*, Penn Central Transp. Co. v. City of New York, 438 U.S. 104, 123-24 (1978). Predictably, the "foreseeability" of future sovereign actions, makes it all the more likely under a reasonable expectation analysis that the private party does not possess vested property rights vis-a-vis the government's exercise of sovereign power. *See, e.g.*, Connolly v. Pension Benefit Guar. Corp., 475 U.S. 211, 227 (1986) ("Those who do business in the regulated field cannot object if the legislative scheme is buttressed by subsequent amendments to achieve the legislative end.") (citing Federal Housing Admin. v. Darlington, Inc., 358 U.S. 84, 146 (1958)); Parkridge Investors Ltd. Partnership v. Farmers Home Admin., 13 F.3d 1192, 1199 (8th Cir. 1994) (it was foreseeable that the government might impair the partnership's contractual options in order to prevent the program's purposes from being foiled); Mitchell Arms, Inc. v. United States, 7 F. 3d 212, 217 (Fed. Cir. 1993) (expectation of selling assault rifles was not a protected property right because it was subject to governmental regulation of firearms importation under the Gun Control Act); Charter Fed. Sav. Bank v. Office of Thrift Supervision, 976 F.2d 203, 212 (4th Cir. 1992) (intent of Bank Board in granting favorable regulatory treatment must be interpreted in light of foreseeably changing regulatory environment), *compare with* Allied-Gen. Nuclear Services v. United States, 839 F.2d 1572, 1577 (Fed. Cir. 1988) (important public safety issues surrounding nuclear proliferation prevents court from supposing that the government was precluded from addressing issue through its licensing power merely because the issue was not originally foreseen). *See also* Jill E. Fisch, *Retroactivity and Legal Change: An Equilibrium Approach*, 110 HARV. L. REV. 1055, 1114 (1997) (change in legal regime should not apply retroactively to contracts previously executed in a climate of regulatory equilibrium).

The question of whether reasonable expectation analysis is appropriate in determining the *existence* of an underlying property interest, as compared to the use restrictions government may impose upon a property owner is beyond the scope of this article. Compare Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 813 (reasonable expectation analysis is an inappropriate factor in establishing the existence of an underlying property right upon which a takings claim may be based) with Lucas v. South Carolina Coastal Council, 505 U.S. 1003, 1026 (1992) (search for inherent restrictions on property owner's title must be guided by traditional understandings of citizens regarding the content of the bundle of rights that they acquire when they obtain title to property).

foreseeable to the parties as an action taken in furtherance of an overall regulatory scheme.[140]

The preceding general analysis would not be complete without addressing two additional points regarding the unmistakability doctrine. First, it should be apparent that the application of the unmistakability doctrine is not inherently limited to the quasi-regulatory model of government contracts. While courts, following the model of *Bowen*, have readily adopted the doctrine to interpret quasi-regulatory agreements, the rule that the government will be presumed to have retained its sovereign authority in contractual dealings is equally applicable to government contracts falling within the market participant model. In these types of routine contracts, the unmistakability doctrine essentially informs the court whether the government has waived its right to assert the sovereign acts doctrine as a defense to an alleged contractual breach.[141] This article will discuss this interaction in more detail in the last section.[142]

Another important aspect of the unmistakability doctrine is the central role it plays in interpreting property rights under quasi-regulatory

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140. One reason for this relationship is that comprehensive regulatory statutes often reserve the power to amend or modify their terms. Courts will generally find such reservations sufficient to incorporate the terms of subsequently enacted legislation into the underlying government contract. *See, e.g.*, Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 53 (1986); National R.R. Passeng. Corp. v. Atchison Topeka Santa Fe Ry. Co., 470 U.S. 451, 467–68, n.22 (1985); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 720 (1878); O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995). *But see* Lynch v. United States, 292 U.S. 571, 577 (1934) (contract provision subjecting insurance policy to all amendments to the original act not sufficient to allow the government to repeal constitutionally its statutory obligation through amendment). Where no statutory reservation exists, courts may still find government contracts subject to the reasonable exercise of sovereign authority. *See, e.g.*, Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 808 (9th Cir. 1990), and cases cited *supra* note 68.

The stark difference between the two sovereign defenses raises a challenge for government contract practitioners as to how best to plead the government's case in a given litigation. For example, arguments made to show that the contract was intended to incorporate later regulatory changes may backfire when new arguments are made as part of the sovereign acts defense regarding the unforeseeability of the subsequent regulatory change. The government lawyers in *Winstar* experienced this dilemma when Justice Souter cited their assertions – that FIRREA's regulatory amendments were *anticipated* by the parties to the contract – in denying the government's sovereign acts defense. *Winstar*, 116 S. Ct. at 2470, n.54; FIRREA, Pub. L. No. 101-73, 103 Stat. 183 (codified as amended in scattered sections of U.S.C.).

141. *See* Hills Materials Co. v. Rice, 982 F.2d 514, 516, n.2 (Fed. Cir. 1992) (Sovereign Acts Doctrine does not prevent the government from affirmatively assuming responsibility for specific sovereign acts). *See also Winstar*, 116 S. Ct. at 2477 (Scalia, J. concurring) (government does not implicitly promise that none of its multifarious sovereign acts will *incidentally* disable it or the other party from performing one of the promised acts).

142. *See infra* notes 335–38 and accompanying text.

contracts. As discussed above, these contracts typically grant private parties limited property rights, which may be modified by the government according to the authorized exercise of sovereign authority. In the quasi-regulatory model, courts employ the unmistakability doctrine to scrutinize claims that the government contract has conferred a constitutionally protected property right that is immune from subsequent exercises of the sovereign power.[143] In these cases, a Fifth Amendment takings claim is appropriate since the government's sovereign, regulatory act directly effects the rights of the private party to the modified regulatory contract. Conversely, Fifth Amendment claims typically do not arise under market participant contracts involving the government's assertion of the sovereign acts doctrine as an excuse for breach. In these cases, the government's liability will normally be due to a court's finding that the alleged "sovereign" act is actually attributable to the government in its "contractual" capacity. Because the government may not "take" property in its role as a pseudo-private contractor, no takings claim arises. Instead, damages are awarded according to common law breach of contract standards. This article will discuss the important potential impacts of *Winstar* on Fifth Amendment takings claims arising under federal contracts in the last section.[144]

2. *Critique of the Supreme Court's Decision in* Winstar v. United States

The Supreme Court's decision in *Winstar* is in some respects probably best understood in the context of the rule that bad law tends to follow from a bad set of facts. Indeed, it is easy to understand the *Winstar* decision on the merits.[145] Government agencies, seeing the coming collapse of the thrift industry and the nearing bankruptcy of the FSLIC, tried to avert a major regulatory overall of the savings and loan industry - as well as the incursion of significant losses to the federal treasury - by inducing solvent banking institutions to merge with bankrupt thrifts in exchange for the promise of favorable regulatory treatment. When that solution produced less than satisfactory results, the government turned an about face, unilaterally withdrew the promised treatment and began foreclosing on their now insolvent contractual partners.

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143. *See* cases cited *supra* note 94.

144. *See infra*, notes 246–84 and accompanying text.

145. Justice Souter's opinion, for example, concludes:
> It would, indeed, have been madness for respondents to have engaged in these transactions with no more protection than the Government's reading would have given them, for the very existence of their institutions would then have been in jeopardy from the moment their agreements were signed.
> *Winstar*, 116 S. Ct. at 2472.

While the Court's decision in favor of the thrifts against the government may be thus applauded, the path it chooses to arrive at its ruling is less commendable. *Winstar*'s problems arise with the Court's initial observation that the "the anterior question of whether there were contracts at all [between the parties] dealing with regulatory treatment of supervisory goodwill and capital credits...is not strictly before us."[146] Beginning from this procedural posture, the Court considers the applicability of the unmistakability doctrine not in terms of contract formation and interpretation but instead as a defense to the thrifts' claims for breach of contract.[147] A second problem for the Court is its failure to make a formal distinction between regulatory agreements and routine market-type contracts. Instead, the Justices take on the arguably impossible task of crafting a set of rules for the government's sovereign defenses that can be applied uniformly to the entire spectrum of government contractual arrangements.

The Court attempts to escape from this procedural box by creating an essentially artificial distinction between claims which attempt to limit sovereign authority and claims for purely monetary damages, leading to the curious - and legally insupportable - result that contractual rights are determined, in part, by the remedy sought by the complaining party (the "remedy test").[148] Applying the remedy test, Justice Souter finds the unmistakability doctrine to be inapplicable to the thrifts' contract claims, which the opinion characterizes as suits for monetary relief rather than attempts to block the sovereign authority of Congress.[149] As a result, the Court's main opinion does not discuss how the unmistakability doctrine should be applied in resolving government contract disputes. The resulting analytical vacuum creates confusion regarding the proper role of the doctrine (including its relationship to the sovereign acts doctrine) and the appropriate "unmistakability" standard. The following sub-sections will discuss each of these problems separately.

a. Problems with the Remedy Test

There are several problems with the remedy test used by Justice Souter to determine whether the unmistakability doctrine should apply to

146. *Winstar*, 116 S. Ct. at 2448. Justice Souter's opinion implies that this issue was not raised in the "questions presented" in the petition for certiorari. *Id.*

147. *Winstar*, 116 S. Ct. at 2448.

148. 116 S. Ct. at 2457-61. In considering whether the unmistakability doctrine should be available as a defense, the Court logically focuses on the policy behind the doctrine, which is to minimize the impact of the government's contractual obligations on the free exercise of its sovereign powers. This emphasis, while understandable, deflects attention from the doctrine's practical function, to establish the parameters for interpretation of what rights and duties arise out of a government contract.

149. 116 S. Ct. at 2458.

interpret government contracts. As an initial matter, it is clear that the test is not well supported by the contract clause precedent from which the unmistakability doctrine is derived. As discussed above, in adopting the unmistakability doctrine from earlier contract clause cases the Supreme Court (and the appellate courts) have ignored the distinction between "reserved" and "non-reserved" powers[150] and instead applied the doctrine equally to all exercises of federal sovereignty.[151] A strong argument can be made, nevertheless, that the reserved powers doctrine applies to the federal government.[152] The assumption that the federal government possesses "non-surrenderable" powers poses a problem, however, for Justice Souter's remedy test, which states that the unmistakability doctrine only applies to determine the conditions under which sovereign power may be surrendered. This reasoning conflicts with the established law of reserved powers, which states that certain essential powers may *never* be surrendered, either expressly or by implication. In the event of such a conflict, one could always respond that the principles of the reserved powers doctrine take precedence. But this approach renders the unmistakability doctrine meaningless as to such reserved powers, a result out of step with the numerous court decisions that have applied the doctrine without making any distinction between "essential" and "non-essential" aspects of federal sovereignty.[153]

The contrary but more logical approach would assume that the unmistakability doctrine applies to limit government assumptions of contractual liability resulting from the exercise of its reserved (as well as its non-reserved) powers. Under this formulation, the reserved powers and unmistakability doctrines complement one another; the first prohibits the actual surrender of the government's reserved power, while the second limits the allocation of liability for the exercise of such power to express contractual language.[154]

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150. *See supra* notes 57-64.

151. *See supra* notes 88-96.

152. As far as this Article is aware, no case has directly addressed this issue. (*But see* cases cited *supra* note 96). It seems apparent, however, that the principles supporting the application of the reserved powers doctrine to the retention of state sovereignty apply with even greater force to the more far reaching sovereign responsibilities entrusted to the federal government.

153. *See* cases cited *supra* note 94.

154. This delineation helps to explain the seeming inconsistency, noted by Justice Souter, *see Winstar*, 116 S. Ct. at 2462, n.34, between Justice Scalia's adoption of the remedy test in regards to the reserved powers doctrine, *see id.* at 2462, and his rejection of the same test in regards to the unmistakability doctrine, *see id.* at 2476. In contrast to its application to the unmistakability doctrine, the remedy test makes sense (at least theoretically) when applied to the reserved powers doctrine, whose sole purpose is to prevent the surrender of the essential sovereign power.

A second problem, described above, is that the remedy test allows parties' rights and duties under a government contract to be determined by the remedy sought by the complaining party. In *Bowen*, for example, the Court applied the unmistakability doctrine to find that the state did not have a compensable property right in the statutory right of withdrawal.[155] Under an interpretive approach less protective of retained sovereign power, however, it is conceivable that the Court could have found the state to have a protected property right in withdrawal from the system, compensable under the Fifth Amendment takings clause.[156]

In this scenario, the existence of a "property right" ultimately depends on the form of remedy sought by the state against the federal government. Such a relationship is, however, legally insupportable. In a contract dispute, the determination of the parties' contractual rights always precedes the remedy analysis, which does not come into play until one party's breach and consequential liability have been established.[157] Justice Souter tries to avoid this problem by stating that the application of the unmistakability doctrine will depend not upon the remedy requested, but rather on a court's interpretation of the terms of the underlying contract. Under the Court's own precedent, however, such contract interpretation requires the application of the unmistakability doctrine in order to establish whether the government waived its right to exercise its sovereign powers

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155. Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 55 (1986). The Court came to this conclusion by interpreting general provisions of the Social Security Act and the underlying 418 agreement to find that the government had not unmistakably waived its right to modify the terms of the state-federal social security contract. *Id.* at 52–56.

156. Under normal rules of contract interpretation, for example, it is possible to imagine the Court characterizing the somewhat general language of the Social Security Act and the § 418 agreement to be mere boilerplate, reserving no effective rights of modification to the government. This is especially true given the common law principle that ambiguous or vague contracts will generally be construed against the party who drafted the contractual provisions. *See, e.g.*, Hills Materials Co. v. Rice, 982 F.2d 514, 516–17 (1992); Fort Vancouver Plywood Co. v. United States, 860 F.2d 409, 414 (Fed. Cir. 1988). *See infra* notes 254–72 and accompanying discussion.

157. *See* 5 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 993 (1964). This point was made by the Federal Circuit Court of Appeals in its first *Winstar* decision, Winstar Corp. v. United States, 994 F.2d 797, 812 (Fed. Cir. 1993), but was ignored by the court's subsequent reversal, 64 F.3d 1531, 1548 (Fed. Cir. 1993), and by the Supreme Court in *Winstar*, 116 S. Ct. 2432. The unmistakability doctrine's role in determining the terms of the underlying contract and whether there has been a breach also distinguishes Justice Souter's remedy test from contracts which assign specific remedies to certain rights that exist in the contract. Such remedy-restricted rights - a party is limited to monetary damages for example - still give rise to a breach of contract, irrespective of whether the relief sought against the breaching party is permitted under the contract.

in the future regarding the subject matter of the contract.[158] By ignoring the role played by the unmistakability doctrine in determining the existence of property rights under a government contract, Souter's opinion backs itself into an untenable legal corner.[159]

Finally, on a less theoretical level, the remedy test fails in its most fundamental objective, to prevent the government's contractual commitments from interfering with the exercise of its sovereign authority. In formulating the remedy test, Justice Souter hints that the test will only preclude the application of the unmistakability doctrine to routine government contracts such as the silk purchase contracts addressed in *Horowitz*.[160] The remedy test does not ensure, however, that the unmistakability doctrine will continue to apply to quasi-regulatory agreements, for which the presumption of reserved sovereign power is most appropriate. As pointed out by both Scalia and Rhenquist, nothing in the remedy test prevents a party from pleading its claims in whatever manner is conducive to avoid the application of the unmistakability doctrine.[161] The Court's previous unmistakability decisions provide limited guidance; in *Bowen* and *Cherokee Nation*, the plaintiffs' claims included actions for pure

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158. *See, e.g.*, United States v. Cherokee Nation of Okla., 480 U.S. 700, 706 (1987); *Bowen*, 477 U.S. at 54-56; National R.R. Passeng. Corp. v. Atcheson, Topeka & Santa Fe Ry. Co., 470 U.S. 451, 467 (1985); Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 148 (1983); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 718 (1878).

159. Justice Rehnquist's dissent points out this conundrum, noting that:

> The plurality justifies its novel departure from existing law by noting that the contracts involved in the present case . . . 'do not purport to bind the Congress from enacting regulatory measures' . . . . But that is precisely what the unmistakability doctrine, as a canon of construction, is designed to determine: *Did* the contract surrender the authority to enact or amend regulatory measures as to the contracting party? If the sovereign did surrender its power unequivocally, and the sovereign breached that agreement to surrender, *then and only then would the issue of the remedy for that breach arise.* (second emphasis added). *Winstar*, 116 S. Ct at 2481.

160. *Winstar*, 116 S. Ct. at 2457-58 (no one would seriously contend that the unmistakability doctrine should apply to the enforcement of humdrum supply contracts); Horowitz v. United States, 267 U.S. 458 (1925).

161. *See Winstar*, 116 S. Ct. at 2477 (Scalia, J., concurring) (virtually every contract operates, in the end, as an assumption of liability in the event of non-performance); *see id.* at 2481 (Rehnquist, J., dissenting) (sophisticated lawyers in the future need only claim money damages based on an alleged government promise to assume the monetary risk of future changes in legislation in order to avoid application of the doctrine). As the dissent notes, the ability of lawyers to alter the terms of contract interpretation by merely rewording their pleading has "an Alice in Wonderland aspect to it." *Id.*

monetary damages.[162] Justice Souter's opinion is sufficiently cognizant of this dilemma to note that merely pleading a damages remedy will not necessarily insulate a party from application of the unmistakability doctrine. Instead, a court must examine whether the claim in fact amounts to a request for an "exemption from the terms of the subsequent statute," tantamount to blocking its effect.[163]

Justice Souter does not spell out how a court is to determine whether a damage claim amounts to an "exemption" from the operation of a sovereign power, nor is it likely that any easy formula is on the horizon. The opinion's own examples, *Cherokee Nation* and *Bowen*, are hardly sturdy precedent. In neither of those cases did the Court even address the effect of the plaintiffs' claims on the exercise of sovereign power.[164] Nor does Justice Souter's interpretation of these cases provide an overall framework of analysis. Souter presents *Bowen* as a perfect example of a damage claim which has the effect of exempting a party from the operation of a statute. In *Bowen*, the lower court found that the appropriate damages for the state's and agencies' claims were equivalent to the amount paid by these parties into the social security fund.[165] Since an award of such damages would have put those parties in the same situation as would an exemption from the statutory amendment eliminating the withdrawal provision, the unmistakability doctrine was correctly applied. *Bowen* is arguably a narrow exception to the rule that money damage claims will normally not block the exercise of a sovereign power, limited to cases in which the appropriate

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162. *See Cherokee*, 480 U.S. 700, 701 (1987) (Cherokee Nation seeks damages and compensation for harm resulting from the assertion of the government's navigational servitude). *See Bowen*, 477 U.S. 41, 49 (1986) (parties alleged that statutory amendment had deprived parties of contract rights without just compensation). *See also Winstar*, 116 S. Ct. at 2481 (Rehnquist, J., dissenting).

163. According to Justice Souter, the analysis should focus on the actual terms of the underlying contract, to establish whether the contract includes "a risk-shifting component that may be enforced without effectively barring the exercise of [the sovereign] power." *Id.* at 2457-58. Souter attempts to characterize *Bowen* as not having relied upon the unmistakability doctrine to reach its holding. *See infra* note 278. A close reading of *Bowen*, however, shows that the Court thought it appropriate to apply the unmistakability doctrine in establishing the "terms" of the state-federal agreement. *See Bowen*, 477 U.S. at 52.

164. In ruling the statutory amendment unconstitutional, the district court in *Bowen* did observe that the state's and state agencies' claims for damages would be "contrary to the will" of Congress. Public Agencies Opposed to Soc. Sec. Entrapment v. Heckler, 613 F. Supp. 558, 575 (E.D. Calif. 1985), *rev'd*, 477 U.S. 41 (1986).

165. As an initial matter, it is not clear why the amounts paid by these parties as social security premiums would be the appropriate measure of damages since, presumably, the parties would still be receiving a reciprocal benefit in the form of social security payments from the federal government.

award of damages corresponds exactly to the requirements that a party would otherwise have to meet under the new regulatory regime.[166]

Souter appears to go further, however, when he characterizes the use of the unmistakability presumption in *Cherokee Nation* as appropriate since "there could be no claim to harm unless the right to be free of the sovereign power to control navigation had been conveyed away by the Government."[167] Taken at face value, this distinction arguably allows the unmistakability doctrine to return (through the backdoor) to the interpretation of quasi-regulatory contracts since, of course, there can never be a claim to harm unless the overriding sovereign power has been conveyed away.[168] However the interpretations fall, Souter's characterization of *Cherokee Nation* shows that a majority on the Court have at least some reservations about simply doing away with the unmistakability presumption in regards to government agreements that clearly implicate the use of sovereign powers. This apparent inclination of the Court does not save the unmistakability doctrine, however, for two reasons.

First, it is unlikely that lower courts, confused as they already will be regarding how to interpret sovereign defenses after *Winstar*,[169] will manage to finesse the subtlety of the Court's language in a manner that consistently preserves the unmistakability presumption for quasi-regulatory contracts. Instead, if one considers the wide variety of legal analyses that make up the federal court decisions that interpreted the effect of FIRREA

166. Other examples which arguably fall within this narrow scope are cases involving sovereign acts which increase annual license fees or royalty rates. *See, e.g., Madera Irrig. Dist. v. Hancock*, 985 F.2d 1397, 1404 (9th Cir. 1993) (court uses unmistakability doctrine to uphold government increase in rates for CVP water supplied pursuant to long term contracts); Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780, 788-89 (D.C. Cir. 1990) (court applies unmistakability doctrine to determine whether lease agreements are subject to Congressional amendment increasing royalty rate on coal mining).

167. *Winstar*, 116 S. Ct. at 2457. Souter goes on to note that "[b]ecause an order to pay compensation would have placed the Government in the same position as if the navigational easement had been surrendered altogether, the holding of Cherokee Nation is on all fours with the approach we describe today." *Id.* at 2457 n.23. Clearly one may anticipate litigation over the meaning of this language in Souter's opinion, which arguably offers the best hope for retaining the unmistakability presumption in quasi-regulatory agreements after *Winstar*.

168. In other words, contract rights that are *subject to* sovereign authority cannot be "harmed" in a contractual sense by the exercise of such sovereign authority. *See infra* notes 237-41 and accompanying discussion regarding the preliminary requirement of establishing a property interest in order to pursue a takings claim.

169. *See infra* notes 188-93 and accompanying discussion.

on rights under forbearance agreements, it is clear the opposite result is a near certainty.[170]

Second, regardless of how the federal judiciary interprets *Winstar*, the mechanics of damage claims brought by private parties under quasi-regulatory agreements will almost surely serve to undermine the unmistakability doctrine. In fact, the *Winstar* Court does not appear to have acknowledged a fairly evident truth; cases involving the determination of property rights arising out of quasi-regulatory contracts almost invariably involve a takings claim for just compensation under the Fifth Amendment.[171] A Fifth Amendment claim for just compensation is exactly the sort of action that, according to Justice Souter, does *not* require application of the unmistakability doctrine.[172] The sovereign power of eminent domain is preserved; the government is simply required to pay out "damages" to the private property owner.[173] Indeed, only if just

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170. Compare the following cases finding for the government: Winstar Corp. v. United States, 994 F.2d 797, 813 (Fed. Cir. 1993); Transohio Sav. Bank v. Office of Thrift Supervision, 967 F.2d 598 (D.C. Cir. 1992); Security Sav. & Loan Ass'n v. Director, Office of Thrift Supervision, 960 F.2d 1318 (5th Cir. 1992); Carteret Savings Bank, FA v. Office of Thrift Supervision, 963 F.2d 567 (3rd. Cir. 1992); Far West Fed. Bank v. Office of Thrift Supervision, 951 F.2d 1093 (9th Cir. 1991); Guar. Financial Servs. Inc. v. Ryan, 928 F.2d 994 (11th Cir. 1991); Franklin Fed. Sav. Bank v. Office of Thrift Supervision, 927 F.2d 1332 (6th Cir. 1991); with the following cases finding for the thrifts: Winstar Corp. v. United States, 64 F.3d 1531 (Fed. Cir. 1993); Transcapital Fin. Corp. v. Office of Thrift Supervision, 44 F.3d 1023 (D.C. Cir. 1994); Resolution Trust v. Federal Sav. & Loan Ins., 25 F.3d 1493 (10th Cir. 1995); Statesman Sav. Holding Corp. v. U.S., 26 Cl. Ct. 904, 920 (Cl. Ct. 1992); *Winstar II*, 25 Cl. Ct. 541; *Winstar I*, 21 Cl. Ct. 112.

171. *See, e.g.*, Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 49 (1986); *Western Fuels-Utah, Inc.*, 895 F.2d at 788; *Cateret Sav. Bank*, 963 F.2d at 583; Allied-General Nuclear Services v. United States, 839 F.2d 1572, 1577 (Fed. Cir. 1988); Parkridge Investors Ltd. Partnership v. Farmers Home Admin., 13 F.3d 1192, 1198-99 (1994). Mitchell Arms, Inc. v. United States, 7 F.3d 312, 217 (Fed. Cir. 1993); Housing Auth. of Fort Collins v. United States, 980 F.2d 624, 630-31 (10th Cir. 1992); Alpine Ridge Group v. Kemp, 955 F.2d 1382, 1385-86 (9th Cir. 1992), *rev'd*, 508 U.S. 10 (1993); Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 810-11 (9th Cir. 1990); *Hughes Communications Galaxy, Inc. v. United States*, 998 F.2d 953, 957 (Fed. Cir. 1993).

172. Several decisions have viewed takings cases as the perfect illustration of how the remedy test may be applied. *See, e.g., Winstar I*, 21 Cl. Ct. at 116 (analogy to remedy test may be found in regulatory takings law, in which the government has the clear authority to regulate extensively, but must pay compensation where such regulation has the result of effectively condemning a property right). *See also* First English Evangelical Lutheran Church v. County of Los Angeles, 482 U.S. 304, 315 (1987) (Fifth Amendment does not limit the governmental interference with property rights per se, but rather secures compensation in the event of an otherwise proper interference amounting to a taking).

173. *See* Ruckelshaus v. Monsanto, 467 U.S. 986, 1016 (1983) (equitable relief is not available to enjoin an alleged taking of private property for public use when a suit for compensation can be brought against the sovereign subsequent to the taking). *Accord Parkridge Investors Ltd. Partnership*, 13 F.3d at 1201. This conclusion is supported by the

compensation damages are found to be inadequate does a private party even have a right to bring an enjoinment action under the Fifth Amendment against the federal government.[174]

One might argue that, in establishing the remedy test, the Court is simply assuming that the threat of just compensation awards will not act as a significant limitation on the exercise of the government's sovereign powers. This assumption is contradicted, however, by the overwhelming anecdotal evidence that the threat of successful takings claims is a strong deterrence to the government's exercise of its regulatory powers.[175] Justice

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realization that, to the extent the reserved powers doctrine applies to the federal government, a government contract could never act to "block the exercise" of the traditionally reserved power of eminent domain. *West River Bridge Co. v. Dix*, 47 U.S. (6 How.) 507 (1848) (holding that eminent domain is a non-surrenderable, reserved power). *See also Winstar*, 116 S. Ct. at 2457 (application of unmistakability doctrine turns on whether enforcement of alleged contractual obligation would block the exercise of the sovereign power). This approach is muddled somewhat by the fact that a government regulatory actions usually "take" property inadvertently, typically according to a legislative authority such as the commerce clause. While it is unclear how a court might untangle this issue, the reserved aspect of the eminent domain power does argue, under the remedy test, against the application of the unmistakability doctrine to takings cases.

174. Under the Tucker Act, 28 U.S.C § 1491 (1994), parties must first bring an action for damages before the claims court before a district court may assume jurisdiction. *See* Preseault v. Interstate Commerce Comm'n, 494 U.S. 1, 11 (1990) (takings claims against the federal government are premature until the property owner has availed itself of the process provided by the Tucker Act); United States v. Riverside Bayview Homes, Inc., 474 U.S. 121, 127-28 (1985) (equitable relief is not available to enjoin an alleged taking when a suit for compensation can be brought against the sovereign); *Ruckelshaus*, 467 U.S. at 1016.

175. *See* Lucas v. South Carolina Coastal Council, 505 U.S. 1003, 1070 n.6 (1992) (Steven, J. dissenting) (costs of increased just compensation damage awards are likely to be substantial and therefore likely to impede the development of sound land-use policy); Nolan v. California Coastal Comm'n, 483 U.S. 825, 866 (1986) (Steven, J., dissenting) (threat of damage awards will have unprecedented chilling effect on public officials charged with the responsibility for drafting and implementing regulations designed to protect the environment); First English Evangelical Lutheran Church v. County of Los Angeles, 482 U.S. 304, 340 (1986) (Stevens, J., dissenting) (cautious local officials and land use planners may avoid taking any action that might later be challenged and thus give rise to a damage action); Agins v. City of Tiburon, 598 P.2d 25, 30 (Cal. 1979), *quoting* Barbara J. Hall, Comment, Eldridge v. City of Palo Alto: *Aberration or New Direction in Land Use Law?*, 28 Hastings L.J. 1569, 1597 (1977) (threat of financial liability will intimidate legislative bodies and discourage the implementation of strict or innovative planning measures in favor of measures which are less stringent, more traditional, and fiscally safe); Allen v. City & County of Honolulu, 571 P.2d 328 (Haw. 1977); Charles v. Diamond, 360 N.E.2d 1295, 1305-06 (N.Y. 1977). *See also* Thomas G. Pelham, *Innovative Growth Control Measures: The Potential Impacts of Recent Federal Legislation and the Lucas Decision*, 25 URB. LAW. 881 (1993); Cotton C. Harness III, Lucas v. South Carolina Coastal Council: *Its Historical Context and Shifting Constitutional Principles*, 10 PACE ENVTL. L. REV. 5, 19 (1992); Charlie R. Wise, *The Changing Doctrine of Regulatory Taking and the Executive Branch: Will Takings Impact Analysis Enhance or Damage the Federal Government's Ability to Regulate?* 44 ADMIN. L. REV. 403, 426

Souter attempts to dodge this objection by stating "the Constitution 'bar[s] Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole.'"[176] The Court does not elaborate on how this general principle of takings law applies to the federal *creation* of property rights,[177] in which the government and private parties enter into voluntary quasi-regulatory agreements governed by generally well settled (at least before *Winstar*) rules of government contract interpretation.

In the final analysis, it is questionable whether the Court considered the potential effect of the remedy test on the determination of property rights under government contracts falling within the quasi-regulatory model. While Justice Souter's opinion may have intended to preserve the unmistakability presumption for the interpretation of quasi-regulatory agreements, the remedy test does not achieve this objective.

Winstar's application of the remedy test effectively precludes a coherent analysis of how the unmistakability doctrine applies to government contract interpretation, how the doctrine relates to the sovereign acts doctrine, and what the substantive "unmistakability" standard should be. The next two subsections will discuss the problems that

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(1992); Lynda L. Butler, *State Environmental Programs: A Study in Political Influence and Regulatory Failure*, 31 WM. & MARY L. REV., 823, 829 (1990); Craig J. Doran, First English Evangelical Lutheran Church of Glendale v. County of Los Angeles *and* Nollan v. California Coastal Commission: *The Big Chill*, 52 ALB. L. REV. 325 (1987); The Supreme Court, 1986 Term Leading Cases, 101 HARV. L. REV. 119, 246 (1987); John Mixton, *Compensation Claims Against Local Governments for Excessive Land-use Regulations: A Proposal for More Effective State Level Adjudication*, 20 URB. LAW. 675, 686 (1988); John E. Cribbet, *Concepts in Transition: The Search for a New Definition of Property*, 1986 U. ILL. L. REV. 1, 36 (1986); Norman Williams, Jr. et al., *The White River Junction Manifesto*, 9 VT. L. REV. 193, 229 (1984); Jonathan B. Sallet, *The Problem of Municipal Liability for Zoning and Land-use Regulation*, 31 CATH. U. L. REV. 465, 478 (1982); Corwin W. Johnson, Compensation for Invalid Land-Use Regulations, 15 GA. L. REV. 559, 594 (1981); Marshall C. Cook, Note, Lucas v. South Carolina Coastal Council: *Low Tide for the Takings Clause*, 44 MERCER L. REV. 1433, 1440 (1993); Natasha Zalkan, Comment, *Shifting Sands and Shifting Doctrines: The Supreme Court's Changing Takings Doctrine and South Carolina's Coastal Zone Statute*, 79 CAL. L. REV. 205, 234–45, 266 (1991); Carl Kirk, Note, *First Church Decides Compensation is Remedy for Temporary Regulatory Takings – Local Governments are "Singing the Blues"*, 21 IND. L. REV. 901 (1988); Kim C. Pflueger, Comment, *Takings Law – Is Inverse Condemnation an Appropriate Remedy for Due Process Violations?* – San Diego Gas & Elec. Co. v. City of San Diego, 450 U.S. 621 (1981), 57 WASH. L. REV. 551 (1982); Alan F. Ciamporcero, Comment, *"Fair" is Fair: Valuing the Regulatory Taking*, 15 U.C. DAVIS L. REV. 741, 748–49 (1982); Marianne Lavelle, *The Property Rights Revolt*, NAT'L. LAW J., May 10, 1993, at 34.

176. *Winstar*, 116 S. Ct. at 2459, *citing Dolan v. City of Tigard*, 512 U.S. 374, 384 (1994), *quoting Armstrong v. United States*, 364 U.S. 40, 49 (1960).

177. *See, e.g., Statesman Sav. Holding Corp. v. United States*, 26 Cl. Ct. at 920 ("purpose animating the unmistakability doctrine makes it clear that the doctrine controls how contractual rights with the government are *created*.") (emphasis added).

arise from this lack of analysis, which is further confounded by the three disparate opinions offered by Justices Souter, Breyer and Scalia.

b. Winstar's Uncertainty Regarding the Proper Role of the Unmistakability Doctrine and its Relationship to the Sovereign Acts Doctrine

At no point in the *Winstar* decision does the Court directly address the function of the unmistakability doctrine, except to characterize the doctrine as a "canon" of contract construction.[178] Belying this characterization, the Court considers the application of the doctrine to contracts whose breach by the government is already assumed, based primarily on factual findings made by the lower court.[179] Since the purpose of the unmistakability doctrine is to determine the existence of underlying contractual rights, the Court's assumption that the thrifts' contractual rights have been breached essentially negates any meaningful application of the doctrine. Instead, the Court asks whether the unmistakability doctrine may be applied to *excuse* the government's breach.[180] Justice Souter's opinion avoids the confusion likely to follow from such an analysis by finding the doctrine inapplicable to the forbearance agreements. The analysis is taken up instead by Justice Scalia who characterizes the doctrine as a rebuttable presumption that the sovereign has made no promise that one of its future acts will prevent it from performing on its contractual obligations.[181] Rather than explicitly stating how he believes the unmistakability doctrine should be applied, Scalia simply upholds the lower court's ruling of breach based upon his own legal conclusion that the government's promises to assume the risk of any future regulatory changes were unmistakable.[182]

The Court's failure to directly address how the unmistakability doctrine should be applied, particularly in a case where the underlying contractual breach is not technically subject to the Court's review,[183] invites uncertainty regarding the doctrine's proper role in resolving government

178. *Winstar*, 116 S. Ct. at 2455.

179. *Id.* at 2452-53 (court accepts Federal Circuit's conclusion that the Government breached the underlying contracts).

180. *Id.* at 2448, 2453.

181. *Id.* at 2477.

182. *Id.* at 2478 (Scalia, J. concurring) ("To be sure, those courts were not looking for "unmistakable" promises . . . but unmistakability is an issue of law that we can determine here."). As a result, Justice Scalia's opinion offers the only guidance to practitioners as to what the Supreme Court might consider the proper "unmistakability standard" to be. *See infra* notes 294-306 and accompanying text.

183. *Winstar*, 116 S. Ct. at 2448 ("[A]nterior question of whether there were contracts at all between the Government and respondents dealing with regulatory treatment of supervisory goodwill . . . is not strictly before us.").

contract disputes.[184] This uncertainty is exacerbated by the Court's failure to distinguish between quasi-regulatory and market participant government contract models, a failure that inevitably blurs the somewhat intricate relationship, as described above, between the unmistakability and sovereign acts doctrines.[185] Both Justice Breyer and Scalia imply that the two doctrines are generally interchangeable.[186] In considering the two doctrines, Scalia observes:

> the 'sovereign acts' doctrine adds little, if anything at all, to the 'unmistakability' doctrine, and is avoided whenever that one would be—i.e., whenever it is clear from the contract in question that the Government was committing itself not to rely upon its sovereign acts in asserting . . . the doctrine of impossibility, which is another way of saying that the Government had assumed the risk of a change in the laws.[187]

The type of confusion that can trickle down from such language may be observed in the Tenth Circuit Court of Appeals decision in *Resolution Trust*

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184. The claims court decisions in *Winstar* illustrate the uncertainty engendered by the unmistakability doctrine (as well as setting the stage for the confusion in the Supreme Court's ultimate analysis.) In its initial decision, *Winstar I*, the claims court used a remedy analysis to find the doctrine inapplicable since the plaintiffs had not sought to enjoin Congress from changing the regulations. 21 Cl. Ct. at 116. After the government requested a clarification, the claims court reheard the case. Without specifically addressing the applicability of the unmistakability doctrine, the court found the existence of a binding contractual promise on the part of the government to provide the plaintiff thrifts with favorable regulatory treatment. *Winstar II*, 25 Cl. Ct. at 549. Subsequently, in *Statesman*, the same court finally addressed the purpose of the unmistakability doctrine which it characterized as controlling "how contractual rights with the government are *created*, i.e. whether the government has agreed in unmistakable terms to be contractually bound." 26 Cl. Ct. at 920 (emphasis added). The court then went on to find that the government had made such an unmistakable commitment. *Id.* at 921. The Federal Circuit Court of Appeals, in upholding the claims court decisions in the consolidated appeal, stated "[w]e agree with, and adopt, the substance of [the claims courts'] analyses," without ever making its own determination of whether the unmistakability doctrine applied. *Winstar Corp. v. United States*, 64 F.3d at 1545. In the end, the Supreme Court Justices appear to believe that the lower courts did not apply the unmistakability doctrine in interpreting the forbearance agreements. 116 S. Ct. at 2478 (Scalia, J. concurring) (lower courts "were not looking for unmistakable promises"); 116 S. Ct. at 2484 (Rehnquist, J. dissenting) ("the trial court and Court of Appeals held the unmistakability doctrine did not apply here.").

185. *See supra* notes 123–40 and accompanying text.

186. Breyer considers the application of the unmistakability doctrine to interpret the parties' respective abilities to raise the commercial impossibility defense. *Winstar*, 116 S. Ct. at 2471–72. He then argues that the "rights and duties" contained in a government contract are governed generally by the law applicable to private parties. *Id.* at 2473. Scalia discusses the unmistakability doctrine in terms of excusing the breach of a party's obligation to perform. *Id.* at 2477.

187. *Id.* at 2478.

Corp. v. Federal Sav. & Loan Ins. Corp.,[188] decided before *Winstar*. In *Resolution Trust*, the court held that FIRREA was not an act of general applicability, as required by the sovereign acts doctrine, and that the sovereign acts doctrine was therefore not available to the government as a defense.[189] Based on this holding, the court dismissed the government's arguments based on the unmistakability doctrine, stating that "[o]nly if the sovereign acts doctrine applied would we be required to address the issue of unmistakability."[190]

As illustrated by *Resolution Trust*, the potential of lower courts, in the absence of Supreme Court guidance, to merge the unmistakability doctrine into the sovereign acts doctrine is quite real.[191] Such a doctrinal entanglement carries potentially significant consequences, however, for the interpretation of rights under the quasi-regulatory contractual model. The sovereign acts doctrine, which wants to treat the government as a private party, does not readily apply to such agreements, entered into by the government as part of a greater regulatory structure.[192] When courts mistakenly apply the sovereign acts doctrine to quasi-regulatory contracts, the result is predictably a denial of relief for the government.[193] If the unmistakability doctrine is considered as merely a sub-part to the sovereign acts doctrine, however, the court's rejection of the government's sovereign act defense also has the effect of eliminating the presumption that such contracts are subject to the exercise of the government's regulatory authority. In a manner similar to the application of Justice Souter's remedy

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188. *Resolution Trust Corp. v. Federal Sav. & Loan Ins. Corp.*, 34 F.3d 982 (10th Cir. 1994).

189. *Id.* at 984.

190. *Id.* at 984. The court's decision freely meshes the requirements of the two doctrines in finding the government liable for breach of contract. *Id.* (court applies "public and general act" requirement of sovereign acts doctrine and remedy distinction (similar to remedy test in *Winstar)* of the unmistakability doctrine). *See also Benjamin v. Jacobson*, 124 F.3d 162, 175 (2d Cir. 1997) ("Where federal government is a party to a contract, a statute modifying the contract will be subjected to the 'sovereign acts' doctrine . . . .").

191. *See also Conoco Inc. v. United States*, 35 Fed. Cl. 309, 335-36 (1996) ("unmistakability doctrine stands and falls with the sovereign acts doctrine" and thus does not apply where government action is not a public and general sovereign act). *Sumner Peck Ranch, Inc. v. Bureau of Reclamation*, 823 F. Supp. 715, 749 (E.D. Cal. 1993) (court applies sovereign acts doctrine to quasi-regulatory agreement).

192. In interpreting such contracts, a court will typically find the sovereign acts doctrine inapplicable, usually due to the direct impact of the government's regulation on contract rights or, in the event of an impossibility defense, the fact that the government act was foreseeable to the contracting parties. *See supra* notes 135–40 and accompanying discussion.

193. *See, e.g., Resolution Trust*, 34 F.3d at 984; *Conoco*, 35 Fed. Cl. at 335–36. This result is due to the general conflict between the requirements of the sovereign acts doctrine, *see supra* notes 99–112 and accompanying discussion, and the characteristics of the quasi-regulatory contractual model, in which the subsequent exercise of sovereign power is often foreseeable and has a significant impact upon underlying contractual rights. *See supra* notes 135–40 and accompanying discussion.

test, this doctrinal merging portends a potentially significant shift in the interpretation of property rights arising under federal regulatory contracts.[194] The effect of this shift on takings claims brought under the Fifth Amendment will be discussed in the next section. The next subsection will discuss a slightly different problem: the uncertainty remaining after *Winstar* as to exactly what the "unmistakability" standard should be.

c. Winstar's Uncertainty Regarding the "Unmistakability" Standard

An additional problem with the *Winstar* opinion is that the Court never arrives at a holding that describes what an "unmistakable" government promise to waive sovereign authority should look like. The confusion is due primarily to the inability of the Court majority's two authors, Justices Souter and Scalia, to agree on whether the unmistakability doctrine applies to the underlying contracts. As a result, both government lawyers and private practitioners are left with ambiguous direction in crafting future contractual arrangements that accurately reflect the true intent of the parties.

Justices Souter and Breyer find that the government made a binding promise to provide favorable accounting treatment to the thrifts based primarily on language in one of the contractual documents stating that resolutions adopted at the time of the thrift mergers (which confer the favorable regulatory treatment) shall take precedence over contrary regulations.[195] Justice Souter notes that this language "tilts in favor of interpreting the contract to lock in the then-current regulatory treatment of supervisory goodwill."[196] As discussed above, however, the Justices do not use the unmistakability doctrine to make this finding. Instead, their long subsequent discussions as to why the doctrine should not apply to the contracts in question lead to the inescapable conclusion that Souter and Breyer do not believe that the government's promises to be bound in the future are "unmistakable."[197]

In contrast, Justice Scalia characterizes the government's promise to accord favorable regulatory treatment as an unmistakable waiver of its sovereign right to change such regulatory treatment in the future.[198] According to Scalia, the unmistakability doctrine does *not* require a party to show a further government commitment not to go back on its original

194. *See supra*, notes 160–77 and accompanying text.

195. *Winstar*, 116 S. Ct. at 2450, 2476.

196. *Id.* at 2450.

197. Souter notes that "[t]o be sure, each side could have eliminated any serious contest about the correctness of their interpretive positions by using clearer language." *Id.* at 2452, n.15. In dissent, Justice Rehnquist notes that surely the unmistakability doctrine must have a role to play in resolving a "serious contest" of contractual interpretation. *Id.* at 2482.

198. *Winstar*, 116 S. Ct. at 2477 (Scalia, J. concurring).

promise.[199] Any other construction would, according to Scalia, make the government's initial promise illusory.[200]

The discrepancy between the standards adopted by the *Winstar* Justices leaves no clear guidelines as to what constitutes an unmistakable promise by the government to be bound by the terms of the original contract. In a later section, this article will attempt to set forth in basic terms a theoretically defensible standard, bearing in mind that the standard itself may depend to an extent on the sovereign power allegedly being surrendered.[201] First, this article will discuss the impact of *Winstar* on takings claims involving federally created property rights.

THE INTERPRETATION OF FEDERAL CONTRACT RIGHTS AFTER *WINSTAR*

The decision in *Winstar* leaves the interpretation of federal contract rights in a state of flux. This is a result of 1) the Court's failure to distinguish between quasi-regulatory and market participant government contractual models; 2) the Court's holding that the unmistakability doctrine will not apply in normal "damage" claims, the usual mode of relief brought by parties seeking compensation for takings of property under the Fifth Amendment; 3) mixed signals from the Court regarding the proper role of the unmistakability doctrine in contract interpretation, including erroneous inferences that the doctrine is merely a first step in applying the sovereign acts doctrine; and 4) the Court's failure to come to an agreement regarding the proper "unmistakability standard." How lower courts will apply *Winstar* to federal contract disputes remains to be seen. It seems likely, however, that *Winstar*, by eliminating the presumption of retained sovereign power in quasi-regulatory contracts, will have a significant impact on how courts approach Fifth Amendment takings claims alleging injury to federally-created property rights. The first part of this section will discuss this potential impact. The second part will present an approach to federal contract interpretation that is better supported by precedent and does not infringe upon the important government responsibility to exercise sovereign power in providing for the general welfare.

1. *The Impact of* Winstar *on Takings Claims Involving Property Rights Acquired Under Quasi-Regulatory Contracts*

In order to understand *Winstar*'s potential impact on takings claims, it is worthwhile to explore the nature of property rights arising under quasi-

199. *Id.*
200. *Id.*
201. *See infra* notes 294-306 and accompanying text.

regulatory contracts and how *Winstar* may effect court decisions involving claims that such rights have been injured as a result of the federal government's exercise of sovereign power.

a. Nature of Quasi-Regulatory Property Rights

Quasi-regulatory property rights differ from "normal" property - such as a fee simple estate - in that they are created through contractual-like arrangements with the federal government.[202] The scope of the right is accordingly delineated by the terms of the statutes and accompanying agreements under which the right is created. In *Bowen*, for example, the State of California had a "right" to withdraw from the social security system, which was subject to the government's right to amend, alter or repeal provisions of the statute and underlying agreement. Under the Mining Law of 1872, miners have a "right" to explore for and develop valuable mineral deposits on the public lands, subject to the government's right to impose reasonable rules and regulations.[203] Water users in the west have a "right" under federal water contracts to water allocations subject to the government's right to alter such contracts consistent with the purposes of the Reclamation Act.[204] Coal miners under the Mineral Lands Leasing Act have the "right" to mine commercial quantities of coal under lease agreements that are subject to the government's right to modify royalty

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202. Court decisions often describe quasi-regulatory agreements in which underlying rights are subject to the exercise of sovereign authority as something less than "contracts." *See e.g.* National R.R. Pass. Corp. v. Atchison Topeka Santa Fe Ry. Co., 470 U.S. 451, 465-67 (1985). (reservations of sovereign power in agreements between government and railroad are "hardly the language of contract"); *Winstar II*, 25 Cl. Ct. at 545 (in Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 52, 54-55 (1986) [no vested rights were created since the basic elements of contract formation were absent]); Alpine Ridge Group v. Kemp, 955 F.2d 1382, 1386 (9th Cir. 1992) (asserted right in *Bowen*, 477 U.S. at 55, was a benefit gratuitously conferred); Orrego v. United States Dep't of Housing and Urban Development, 701 F. Supp. 1384, 1396-97 (N.D. Ill. 1988) (cites *Bowen* for proposition that prepayment provision is simply part of a regulatory program over which Congress retained authority to amend in the exercise of its power to provide for the general welfare). Essentially, these decisions equate the term "contract" with an agreement that confers unqualified, constitutionally protected rights on the private party. This section will nevertheless refer to all quasi-regulatory agreements as "contracts" or "contractual arrangements" without necessarily assuming that the underlying statutory schemes create vested property interests protected under the Fifth Amendment. It is clear that the language of the cases, as well as the value of non-vested contractual rights, support the notion that a government contract may in fact be formed without necessarily conferring unalterable vested rights. In the last analysis, whether one refers to an agreement between the government and a private party as a "contract" or not, the unmistakability doctrine still plays a role in determining the rights of the respective parties.

203. 30 U.S.C. § 22 (1994).

204. 43 U.S.C. §§ 371-573 (1994); *see* O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995); Madera Irrig. Dist. v. Hancock, 985 F.2d 1397, 1404, 1406-07 (9th Cir. 1993).

rates and readjustment time intervals.[205] State student loan agencies have the right to receive reimbursements for defaulted loans and other payments by the federal government, subject to the government's right to amend the terms of the guaranteed student loan program.[206] Many other examples may be given, covering a wide range of contractual rights.[207]

Undoubtedly one of the most complex issues in federal contract interpretation is the nature of the property interests that are created by the various regulatory agreements entered into between the government and private parties. Most court decisions interpret such federally-created rights in the context of takings claims; parties argue that government actions have extinguished their "rights" and thus taken "property" in violation of the Fifth Amendment.[208] As a result, most judicial definitions of "property" turn on whether the government may extinguish the right, through regulation or otherwise, without paying compensation. If the government may not do so, the right is said to be "vested" and considered to be a valid, constitutionally protected "property interest."[209] In cases where courts find that the government may eliminate the "right," no "property interest" arises.

The issue of how *Winstar* effects the judicial interpretation of quasi-regulatory contract rights in takings cases is one of the central themes of this

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205. 30 U.S.C. §§ 181-287 (1994); Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780, 789 (D.C. Cir. 1990); *see also* Western Energy Co. v. Dep't of Interior, 932 F.2d 807 (9th Cir. 1991); Trapper Mining Inc. v. Lujan, 923 F.2d 774 (10th Cir. 1991); Coastal States Energy Co. v. Hodel, 816 F.2d 502 (10th Cir. 1987); FMC Wyoming Corp. v. Hodel, 816 F.2d 496 (10th Cir. 1987).

206. *See* Association of Accredited Cosmetology v. Alexander, 979 F.2d 859, 867 (D.C. Cir. 1992); Rhode Island Higher Educ. Assistance Auth. v. Secretary U.S. Dep't of Educ., 929 F.2d 844, 850-51 (1st Cir. 1991); Great Lakes Higher Educ. Corp. v. Cavazos, 911 F.2d 10, 16 (7th Cir. 1990); Educational Assistance Corp. v. Cavazos, 902 F.2d 617, 629, n.20 (8th Cir. 1990); Ohio Student Loan Comm'n v. Cavazos, 900 F.2d 894, 901-02 (6th Cir. 1990); South Carolina State Educ. Assistance Auth. v. Cavazos, 897 F.2d 1272, 1275-76 (4th Cir. 1990).

207. *See e.g.* Federal Housing Admin. v. Darlington, Inc., 358 U.S. 84 (1958); Parkridge Investors Ltd. Partnership v. Farmers Home Admin., 13 F.3d 1192 (8th Cir. 1994); Housing Auth. of Fort Collins v. United States, 980 F.2d 624 (10th Cir. 1992) (regulation of low income housing); Mitchell Arms, Inc. v. United States, 7 F. 3d 212 (Fed. Cir. 1993) (regulation of firearms importation); Allied-General Nuclear Serv. v. United States, 839 F.2d 1572 (Fed. Cir. 1998) (regulation of nuclear power industry).

208. *See e.g.* Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 49 (1986) (public agencies claim statutory amendment deprived them of contractual rights without just compensation in violation of the Fifth Amendment); *Western Fuels-Utah, Inc.*, 895 F.2d at 788 (lessees argue that Congressional readjustment of royalty rate takes property without just compensation); Carteret Sav. Bank v. Office of Thrift Supervision, 963 F.2d 567, 583 (3rd. Cir. 1992) (thrift argues that abrogation of contract right to treat supervisory goodwill as regulatory capital constitutes a taking without just compensation).

209. *See, e.g.*, Lynch v. United States, 292 U.S. 571, 579 (1934) ("Rights against the United States arising out of contract with it are protected by the Fifth Amendment.").

article and will be returned to in the next sub-section. At this point, however, it is worthwhile to observe that the vested rights approach to defining "property interests," while specifically appropriate for takings cases, does not present the complete scope of contractual rights arising out of quasi-regulatory contracts. A closer examination reveals at least three contexts in which these federally created rights may have value and importance to the right holder, while still not rising to the level of "vested" property.[210]

The first context addresses the nature of the right against third parties. Water appropriations in California are a good illustration of "third party" value. The government may exercise enormous regulatory control over appropriative water rights; where the appropriation is found to be wasteful or unreasonable, the right may be eliminated altogether.[211] While the extent of the government's regulatory power makes it less likely that appropriative rights would be considered "vested" for purposes of takings analysis, the rights are still exclusive as to third parties, and thus tremendously valuable to the holder. This value is memorialized by strict priority systems[212] such that, in times of shortage, junior water users may be required to relinquish their water diversions in order for senior appropriators to receive their full allotment.[213]

A second context addresses the "temporal value" of the right. Temporal value can be characterized as the value of a contractual right for the time it exists prior to modification by the government. In *Western Fuels-Utah, Inc. v. Lujan*, for example, the court held that coal lessees holding indefinite term leases did not have a vested right to continue to pay royalties of 5 cents per ton of coal extracted, and thus no "property interest" was taken when Congress raised the royalty rate to 12.5 cents per ton.[214] This holding, however, did not prevent the lessees from having enjoyed the contractual right to mine coal at 5 cents per ton for many years prior to the

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210. For purposes of this article, "vested property" will refer to property which is not "qualified by" or "subject to" the exercise of sovereign power.

211. *See, e.g.*, Joslin v. Marin Mun. Water Dist., 429 P.2d 889, 898 (Cal. 1967); CAL. CONST. art. X, § 2; CAL. WATER CODE §§ 100, 275 (West 1971); *see also* Coffin v. Left Hand Ditch Co., 6 Colo. 443 (1882).

212. *See, e.g.*, CAL. WATER CODE § 1450 (West 1971).

213. *See, e.g.*, Joerger v. Pacific Gas & Elec. Co., 276 P. 1017, 1026 (Cal. 1929); United States v. State Water Resources Control Bd., 227 Cal. Rptr. 161, 188, n.25 (Cal. Ct. App. 1986).

214. 895 F.2d 780, 789 (D.C. Cir. 1990); *See also* Western Energy Co. v. Dep't of Interior, 932 F.2d 807 (9th Cir. 1991); Trapper Mining Inc. v. Lujan, 923 F.2d 774 (10th Cir. 1991); Coastal States Energy Co. v. Hodel, 816 F.2d 502 (10th Cir. 1987); FMC Wyoming Corp. v. Hodel, 816 F.2d 496 (10th Cir. 1987).

congressional amendment.[215] While the temporal value of this right did not rise to the level of Fifth Amendment "property" when confronted with federal legislation, it had undoubtedly been a valuable interest, subject to sale or use as loan collateral, during the time of its existence.[216]

A third context addresses the value of the right vis a vis government actions to which the right is not subject. In a quasi-regulatory contract, rights will not be considered "vested" property interests if they are subject to the future exercise of the government's sovereign powers. The same rights are constitutionally protected, however, from government actions that are unreasonable or inappropriate to the public purpose justifying their adoption.[217] In addition, contractual rights may be immune from legislation or agency actions that do not arise out of the underlying statute which created the contractual right in the first place. A good example of this may be found in the 1872 Mining Act.[218] Under this Act, miners who discover valuable mineral deposits obtain exclusive rights to mine a claim, subject to reasonable rules and regulations.[219] As a result of judicial interpretation, authorized federal regulations that render a mining operation unprofitable extinguish the "property interest" in the miner's

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215. The cases do not elaborate on how long the lessees held their leases prior to the Congressional amendments in 1976. The 5 cents per ton royalty rate was part of the original statute passed in 1920. Theoretically then, the lessees could have enjoyed 46 years of 5 cent royalties, despite the "tenuous" status of this contractual right before the exercise of federal sovereign power. The "temporal value" of a contractual right is protected from the retroactive exercise of sovereign power by the holding in *Sinking Fund Cases* that the government's reserved power does not include the right to "unmake contracts that have already been made . . . ." Union Pac. R.R. Co. v. United States, 99 U.S. 700, 721 (1878). *See* Yankee Atomic Electric Co. v. United States, 33 Fed. Cl. 580, 584–85 (1995), *rev'd on other grounds*, 112 F.3d 1569, 1573–75 (Fed. Cir. 1997) (court finds that government assessment against utilities for cleanup expenses did not constitute retroactive increase in the price of the government's prior contractual agreements). *See infra* notes 326–33 and accompanying discussion.

216. For a similar example in the framework of federal water rights, see Madera Irrig. Dist. v. Hancock, 985 F.2d 1397, 1403 (9th Cir. 1993). *Madera* presents an interesting example of the temporal value of a non-vested contractual right. *See infra* note 327; *see also Winstar*, S. Ct. at 2484 (Rehnquist, J., dissenting) (where government agreed to certain regulatory treatment only for the short term, thrifts still received consideration).

217. United States Trust Co. v. New Jersey, 431 U.S. 1, 22 (1977). *See also* Home Bldg. & Loan Ass'n. v. Blaisdell, 290 U.S. 398, 438-39 (1934) (question is whether the legislation is addressed to a legitimate end and measures taken are reasonable and appropriate to that end); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 721 (1878) (modifications of contract must be consistent with object and scope of authorizing statute). *See infra* notes 307–33 and accompanying text for a more detailed discussion of limits on federal power to modify contractual rights under quasi-regulatory contracts.

218. 30 U.S.C. §§ 21-54 (1994).

219. 30 U.S.C. § 22 (1994); United States v. Locke, 471 U.S. 84 (1985).

claim, without violating the Fifth Amendment.[220] In contrast, if the federal government instead eliminates the miner's claim by declaring the lands off limits to mining, the resulting withdrawal will be found to violate the miner's rights under the Fifth Amendment, since the congressional power of withdrawal is not incorporated into the statutory limits placed on the property interest found within the unpatented claim.[221]

Each of these three contexts operate simultaneously to give value to federal contractual rights that may nevertheless not be considered vested "property" by a court addressing their validity in the face of the government's exercise of sovereign authority. In California, federal water rights created by the Central Valley Project (CVP) illustrate this principle. Under a standard CVP water contract, a water user is entitled to a specific annual allotment of water, which is enforceable against other consumptive users in the system, according to the priority of the water right held by the Bureau of Reclamation.[222] CVP contracts may be modified by Congress pursuant to amendments to the Reclamation Act or, arguably, pursuant to valid exercises of sovereign authority under laws such as the Endangered Species Act.[223] In the absence of such modifications, however, a water user may continue to receive the benefits of the contract. In the event Congress or the Bureau of Reclamation intentionally eliminates such benefits pursuant to legislation that is outside the public purposes of the Reclamation Act, the water user would presumably be entitled to compensation under the Fifth Amendment.[224]

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220. *See* 30 U.S.C. § 22 (1994); Michael Graf, *Application of Takings Law to the Regulation of Unpatented Mining Claims*, 24 ECOLOGY L.Q. 57, 112-115 (1997).

221. *See* Graf, *supra* note 220 at 119-21. Note that a different analysis might ensue if the sovereign action was an unforeseeable event which otherwise satisfied the criteria for excusing government liability under the sovereign acts doctrine. *See infra* notes 309–12 and accompanying text.

222. *See, e.g.*, United States v. State Water Resources Control Bd., 227 Cal. Rptr. 161, 188, n.25 (Cal. Ct. App. 1986); Brian Gray, *The Modern Era in California Water Law*, 45 HASTINGS L.J. 249, 279 (1994).

223. *See infra* notes 309–10 and accompanying text; O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995).

224. For example, if the Bureau of Reclamation pursuant to an amendatory statute or regulations were to ship its water to urban users willing to pay more per acre foot, at the expense of agricultural contract holders, a court could arguably find a constitutional taking, since the Bureau's action would be outside the stated public purpose of the Reclamation Act, to create a pattern of family held farms through the delivery of federally subsidized water. *See, e.g.*, Ivanhoe Irrig. Dist. v. McCracken, 357 U.S. 275, 292 (1958); Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 803, n.8. (9th Cir. 1990). (*See also* Union Pac. R.R. Co. v. United States, 99 U.S. 700, 721 (1878) (amending statute must be consistent with purpose of authorizing statute). An even more difficult question is presented if the Bureau's action is taken pursuant to a newly enacted separate statute establishing a different, but arguably equally valid, public purpose of delivering water to cities and suburbs at the expense of agriculture.

The realization that "non-vested" rights arising out of federal government contracts may have great value to private parties forms a response, in part, to judicial language, such as Justice Scalia's opinion in *Winstar*, that characterizes government promises subject to the exercise of future sovereign authority as "illusory" and agreements containing such promises as more "regulatory" than contractual in nature.[225] Such a characterization ignores the "property-like" aspects of these contractual rights over their period of existence vis a vis third parties and government actions not taken in a sovereign capacity or otherwise unreasonable in light of the public purposes underlying the contract in question.[226] For purposes of this article, the characterization also offers an erroneous portrayal regarding the effect of the unmistakability doctrine on quasi-regulatory contractual rights. The unmistakability doctrine subjects these rights, absent express language to the contrary, to the future exercise of sovereign power. If one considers such "conditional" rights to be valueless, one may thus adopt the view that the mere application of the unmistakability presumption has the potential to extinguish the private party's underlying "property" interest in the quasi-regulatory contract.[227] This analysis presents a false dichotomy, for (as discussed above) rights subject to future sovereign powers may still have important "property-like" aspects.[228] Notwithstanding its potentially misleading characterization, the "vested right" property approach understandably creates a disincentive for courts to apply the unmistakability doctrine to interpret private contractual rights that judges may, on equitable grounds, have no desire simply to eliminate.[229] This article will return to this

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Another complicated issue is whether the government should be held responsible as a quasi-sovereign delivering water under the federal CVP program, for unforeseen sovereign acts that prevent the government from delivering the promised contractual allotments. In other words, should the government be allowed to raise, in certain situations, what amounts to a sovereign acts defense even if the government is contracting under the quasi-regulatory government contractual model? Moreover, how should actions taken under statutes such as the Endangered Species Act be treated in such an analysis? *See infra* notes 307-19 and accompanying text for a discussion (if not a resolution) of these difficult issues.

225. *Winstar*, 116 S. Ct. at 2477.

226. *See Madera Irrig. Dist. v. Hancock*, 985 F.2d 1397, 1405 (government like any other contracting party may enter into a binding agreement subject to a qualified right of modification or other avoidance of obligations) (citing Modern Sys. Tech. Corps v. United States, 24 Cl. Ct. 699, 701, n.3, (1992) aff'd 980 F.2d 745 (Fed. Cir. 1192)).

227. This reasoning is based upon the theory that the "property" status of federal contractual rights turns on whether the unmistakability doctrine subjects such rights to the exercise of future sovereign power.

228. *See supra* notes 210-24 and accompanying text.

229. The various *Winstar* decisions illustrate the reluctance of the judiciary to presume that the government may change the law where it appears to the court that such an interpretation will eliminate the private party's initial contractual rights. *See Winstar*, 116 S.

theme in the last section that discusses how the unmistakability doctrine should be applied.[230]

b. Takings Law and Rights Under Quasi-Regulatory Contracts

The takings clause to the Constitution prohibits the taking of private property for public use without payment of just compensation.[231] While the takings clause historically protected property from physical invasion by the government,[232] the twentieth century has seen the rise of "regulatory takings" law, in which a party claims that government regulation has reduced the value of a property interest so significantly as to constitute the equivalent of a physical occupation.[233] The question of how far a regulation may go before it requires the payment of just compensation was first addressed by the Supreme Court in 1922,[234] and has been the subject of considerable debate ever since.[235] The most comprehensive, recent Supreme Court takings decision is *Lucas v. South Carolina Coastal Council*.[236] In *Lucas*, the Court adopted a per se rule that a statute which deprives a landowner of all economically viable use of his land requires compensation, regardless of whether or not the statute was enacted for a legitimate public

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Ct. at 2472 (it would have been madness for thrift to enter into agreements subject to retention of sovereign power to change the law).

230. *See infra* notes 287-329 and accompanying text.

231. U.S. CONST. amend. V.

232. *See, e.g.*, Loretto v. Telepromptor Manhattan CATV Corp., 458 U.S. 419, 434-435 (1982) (government action constituting permanent physical occupation of property constitutes automatic taking without regard to important public purpose of regulation or extent of economic impact); Loveladies Harbor, Inc. v. U.S., 28 F.3d 1171, 1175 (Fed. Cir. 1994).

233. A regulatory taking case is thus defined as an action in "[in which] the value or usefulness of private property [has been] diminished by regulatory action not involving the physical occupation of the property." Hall v. City of Santa Barbara, 833 F. 2d 1270, 1275 (9th Cir. 1986).

234. Pennsylvania Coal Co. v. Mahon, 260 U.S. 393, 415 (1922).

235. *See, e.g.*, Dolan v. City of Tigard, 512 U.S. 374, 384 (1994); Lucas v. South Carolina Coastal Council, 505 U.S. 1003 (1992); First English Evangelical Lutheran Church v. County of Los Angeles, 482 U.S. 304 (1987); Nolan v. Coastal Comm'n, 483 U.S. 825, 837 (1987); Keystone Bituminous Coal Ass'n. v. DeBenedictis, 480 U.S. 470 (1986); Agins v. City of Tiburon, 447 U.S. 255 (1980); Penn Central Transp. Co. v. New York City, 438 U.S. 104, 123-24 (1978).

236. 505 U.S. 1003 (1992). Two earlier decisions from 1987 had signaled the Supreme Court' s conservative shift in takings cases, foreshadowing its decision in *Lucas*. In *Nolan v. Coastal Comm'n*, the Court found that a coastal commission decision requiring a public easement on a landowner's beachfront estate as a condition of approval for remodeling failed to satisfy the requisite "nexus" between the condition imposed and the original purpose of the building restriction and that the restriction was thus not a legitimate purpose under the police power. 483 U.S. at 831. In *First English Evangelical Lutheran Church v. County of Los Angeles*, the Court held that a claimant may recover damages for a temporary taking of property during the time period in which a regulation ultimately found to be unconstitutional is being challenged. 482 U.S. at 318-19.

purpose.[237] The Court stated an exception to its per se rule, however, where the property interests proscribed by the regulation were "not part of [the owner's] title to begin with."[238]

The holding of *Lucas* emphasizes that an essential preliminary step in takings analysis is to examine the scope of the underlying property interest alleged to have been taken. In *Lucas*, the underlying source of the fee simple property was state law. Thus, the scope of the property interest could only be limited by "restrictions that background principles of the State's law of property and nuisance already place upon land ownership."[239] After opining that the state's general police power authority to protect and preserve its beaches did not likely fall within the narrower power to control nuisances,[240] the Court remanded the case back to the South Carolina Supreme Court to determine whether the State's building prohibition had "taken" the underlying property.[241]

In *Lucas*, the Court accepted as a finding of fact the ruling of the South Carolina Supreme Court that the state beach protection ordinance had completely eliminated all uses of the property alleged to have been taken. Similarly, takings claims involving rights arising under quasi-regulatory contracts typically assume that the government action has eliminated the alleged property right.[242] Instead, as in *Lucas*, the question becomes whether the asserted right is subordinated to the exercise of the government power. In federal contract interpretation, courts will answer this question by examining the language of the authorizing statute and underlying contractual agreement.[243] While the range of different contractual rights arising out of such arrangements is as varied as the "wide spectrum"[244] of statutory purposes, the end analysis is always the same; if

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237. 505 U.S. at 1019–1024.

238. *Id.* at 1026. The Court also noted in a footnote that a landowner who does not suffer total economic deprivation by a regulation may still have a takings claim depending upon the economic impact of the regulation and the degree to which the regulation interferes with distinct investment-backed expectations. *Id.* at 1019 n.8

239. *Id.* at 1028.

240. *Id.* at 1030; *Penn Cent. Transp. Co.*, 438 U.S. at 145 (Rehnquist, J., dissenting) ("Nuisance exception to the takings guarantee is not coterminous with the police power itself.").

241. 505 U.S. at 1030. The case was subsequently settled by the State's purchase of Lucas' beachfront lot for $1 million.

242. This result is usually due to the contracting party's characterization of the "interest" eliminated by the government regulation as a "property" right. *See, e.g.*, Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 51 (1986) (state characterizes contractual right to withdraw as "private property"); *see infra* notes 320–25 and accompanying text.

243. *See* cases cited *supra* note 95.

244. *Winstar*, 116 S. Ct. at 2457.

the right is subject to the government power alleged to have extinguished the right, no taking will be found.[245]

c. Winstar's *Impact on Takings Claims Involving Quasi-Regulatory Contracts*

Winstar changes the mechanics of federal contract takings claims by significantly limiting the applicability of the unmistakability presumption in interpreting property rights under quasi-regulatory agreements. Under *Winstar*'s remedy test, takings claims for just compensation arising out of quasi-regulatory agreements will not act to block the effect of the government action and thus the unmistakability doctrine will not apply.[246] The Court's blurring of the distinctive roles of the unmistakability and sovereign acts doctrines also has the potential to eliminate the unmistakability presumption from the interpretation of quasi-regulatory agreements.[247] Where the two doctrines are considered together, a court will not apply the presumption in regulatory settings to which the assertion of the sovereign acts doctrine is inappropriate.[248]

The elimination of the unmistakability doctrine from the interpretation of rights under quasi-regulatory agreements amounts to a significant power shift away from the government's sovereign authority and towards the property rights of private contractors. As discussed above, the unmistakability doctrine creates a presumption that contractual rights under federal contracts are subject to future sovereign authority, which can only be rebutted by "unmistakable" language to the contrary.[249] Under *Lucas*, a quasi-regulatory contractual right that is subject to the government's sovereign power may be extinguished by the exercise of such power without violating the Fifth Amendment.[250] This is so because, unlike the fee simple real property estate, the property interest contained within the contractual right does not exist outside of the government's sovereign

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245. *See, e.g.*, United States v. Cherokee Nation of Okla., 480 U.S. 700, 707 (1987); *Bowen*, 477 U.S. at 52; Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 812–13 (10th Cir. 1990); *See also* Mineral Lease cases: Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780, 789 (D.C. Cir. 1990); cases, *supra* note 115; Student Loan Cases: Association of Accredited Cosmetology v. Alexander, 979 F.2d 859, 867 (D.C. Cir. 1992); cases, *supra* note 116; Housing cases Parkridge Investors Ltd. Partnership v. Farmers Home Admin., 13 F.3d 1192, 1199 (8th Cir. 1994); cases, *supra* note 117.

246. *See supra* notes 171–74 and accompanying text.

247. *See supra* notes 192–94 and accompanying text.

248. *See, e.g.*, Resolution Trust Corp. v. F.S.L.I.C., 34 F.3d 982, 983 (10th Cir. 1994); Conoco v. United States, 35 Fed. Cl. 309, 335–36 (1996).

249. *See supra* notes 70–88; *See also infra* notes 294–306 and accompanying text for a more detailed discussion of the actual unmistakability standard.

250. 505 U.S. at 1018–25 (property interests not part of owner's original title may be eliminated through regulation).

authority. The logic of this result has been followed by the many cases, decided before and after *Lucas*, that have applied the unmistakability doctrine to find no compensable property interest under various quasi-regulatory contracts.[251]

The inevitable result of not applying the unmistakability doctrine in interpreting such contracts will be that, in many cases, quasi-regulatory contractual rights will no longer be "subject to" the exercise of the government's sovereign powers. Under *Winstar*, these contractual rights will thus rise to a level approaching that of the fee simple estate in *Lucas*, ultimately superior in constitutional status to the government's police power.[252] This conclusion is relatively straightforward when one considers that, in the absence of the unmistakability presumption, the government is treated as any other private party in its contractual dealings.[253] In this event, two generally applicable principles of contract interpretation will work against the government's argument that it has contractually reserved the future right to exercise its sovereign powers.

The first principle states that ambiguous language will be interpreted against the party which wrote the contract.[254] The second principle holds that general "boilerplate" provisions in an agreement will be treated with limited deference by a court and will always be overruled

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251. *See supra* notes 95, 158 and cases cited therein. In *Great Lakes Higher Educ. Corp. v. Cavazos*, 711 F. Supp. 485, 495 (W.D. Wis. 1989), the district court cited *Bowen*, 477 U.S. 41 (1986), for the proposition that "an amendment that changes the terms of agreements expressly subject to statutory change does not violate the Fifth Amendment, even if it is applied retrospectively."

252. The general rule of takings law that "economic rights" are subject to a slightly lesser standard of Fifth Amendment protection will prevent such contractual rights from ever rising to the same level of constitutional protection as the fee simple interest in real property. *See, e.g., Lucas v. South Carolina Coastal Council*, 505 U.S. at 1026-29 (1992) (commercial property rights subject to greater regulatory authority by state); United States v. Locke, 471 U.S. 84, 105 (economic rights derived from mining claim subject to substantial government regulatory authority); Andrus v. Allard, 444 U.S. 51, 64-66 (1979) (government retains substantial power to regulate commercial property interests).

253. *Winstar*, 116 S. Ct. at 2473 (Breyer, J., concurring). *See also* Perry v. United States, 294 U.S. 330, 352 (1935); Lynch v. United States, 292 U.S. 571, 579 (1934); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 719 (1878).

254. *See* United States v. Seckinger, 397 U.S. 203, 216 (1970); Hills Materials Co. v. Rice, 982 F.2d 514, 516-17 (Fed. Cir. 1992); Fort Vancouver Plywood Co. v. United States, 860 F.2d 409, 414 (Fed. Cir. 1988); *United Int'l Investigative Servs. v. United States*, 33 Fed. Cl. 363, 370 (Fed. Cl. 1995) *rev'd on other grounds*, 109 F.3d 734 (Fed. Cir. 1997); Conoco Inc. v. United States, 35 Fed. Cl. 309, 326 (Fed. Cl. 1996). *See also* RESTATEMENT (SECOND) OF CONTRACTS § 206 (1981) (when contract language is ambiguous, that meaning is generally preferred which operates against the party who supplies the words or from whom a writing otherwise proceeds).

by more specific contractual language.[255] Taken together, these principles spell trouble for the preservation of the government's sovereign authority based on general provisions inserted into the agreement by the government. As an example, numerous decisions such as *Sinking Fund Cases, National Railroad,* and *Bowen* have used the unmistakability doctrine to interpret general reservation language (that Congress reserves its right to amend, alter or repeal the authorizing statute) as superseding more specific promises found within the contractual agreements. Under normal principles of contract interpretation, however, any of these cases could have gone the other way.[256] Another example are the general provisions found in government contracts that limit governmental liability. Private party contract interpretation tends to interpret such provisions as "force majeure" clauses,[257] which shield a party from liability only for unforeseen, unanticipated events.[258] In highly regulated fields, the "force majeure" interpretation would tend to hold the government responsible for subsequent regulatory enactments, most of which would be arguably foreseeable to the contracting parties.[259]

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255. *See e.g.* Hughes Communications Galaxy v. United States, 998 F.2d 953, 957-58 (Fed. Cir. 1993); Hills Materials Co. v. Rice, 982 F.2d 514, 517 (Fed. Cir. 1992); United States v. Johnson Controls, Inc., 713 F.2d 1541, 1555 (Fed. Cir. 1983); Hol-Gar Mfg. Corp. v. United States, 351 F.2d 972, 979-80 (Ct. Cl. 1965); Conoco Inc., 35 Fed. Cl. at 322-23; *United Int'l Investigative Servs.*, 33 Fed. Cl. at 370.

256. *See, e.g., Hughes Communications Galaxy,* 998 F.2d at 957-58 (specific contractual clause takes precedence in interpreting parties' intent over general clauses which subordinate the contract to unspecified United States obligations, law and policy).

257. "Force majeure" is alternatively defined as an "act of God", an "irresistible force," or "an event that cannot be definitely foreseen or controlled." *See, e.g., Moncrief v. Williston Basin Interstate Pipeline Co.*, 850 F. Supp. 1495, 1508 (D. Wyom. 1995); Joan Teshima, Annotation, *Gas and Oil Lease Force Majeure Provisions: Construction and Effect,* 46 A.L.R. 4th 976 § 2(a) (1987).

258. *See* Eastern Air Lines, Inc. v. McDonnell Douglas Corp., 532 F.2d 957, 990 (5th Cir. 1976) ("Exculpatory provisions which are phrased merely in general terms have long been construed as excusing only unforeseen events which make performance impracticable."); *Moncrief,* 850 F. Supp. at 1508 (force majeure describes an event that cannot be foreseen or controlled). *See also Nugget Hydroelectric, L.P. v. Pacific Gas & Elec.*, 981 F.2d 429, 432 (9th Cir. 1992).

259. *See, e.g., Winstar,* 116 S. Ct. at 2471 (there is no doubt that some changes in the regulatory structure governing thrift capital reserves were both foreseeable and likely). In one sense, the "force majeure" interpretation renders government's position similar to the impossibility defense raised under the sovereign acts doctrine, i.e., the government should be excused from liability only for sovereign acts that are contrary to the assumptions under which the parties originally contracted. *See, e.g.*, Commonwealth Edison Co. v. Allied-General Nuclear Serv., 731 F. Supp. 850, 855 (N.D. Ill. 1990) (standard, boilerplate, catch-all force majeure provision invokes a body of common law doctrine interpreting the term that is largely indistinguishable from the doctrine of impossibility). *See supra* note 39.

A good illustration of how the elimination of the unmistakability doctrine from federal contract interpretation may enlarge the rights of private parties against the government[260] can be found in the satellite cases, *Hughes Communications*[261] and *American Satellite*.[262] The satellite cases arose due to the government's decision, following the shuttle Challenger tragedy in 1986, to eliminate commercial launches from NASA's space program. Prior to that time, private businesses had contracted with NASA for commercial launches of various products according to standard launch service contracts.[263] As a result of the Challenger crash, the President issued a new order which effectively precluded most, if not all, of the plaintiffs' commercial launches from occurring.[264] The plaintiffs brought claims for breach of contract and Fifth Amendment takings against the government. The claims courts found for the government, holding that contractual provisions that subjected the parties to United States obligations, law and published policy incorporated the government's sovereign powers into the terms of the contract.[265] Accordingly, the plaintiffs' contractual rights were subject to future policy changes regarding the U.S. space program and thus no takings could have occurred.[266]

The appellate court reversed the claims court rulings based on the reasoning that these general contract reservations were superseded by more specific contractual language in which the government promised to provide launch services according to United States policy signed by the President

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260. Another case that illustrates this principle is Hills Materials Co. v. Rice, 982 F.2d 514 (Fed. Cir. 1992). In *Hills*, a contractor claimed that the government was responsible for increased costs due to post-bid changes in regulations. The contractor relied on a contractual provision that required the contractor to "[c]omply with the standards issued by the Secretary of Labor at 29 CFR part 1926 . . . ." 982 F.2d at 516. Based on this language, the contractor argued that the term "issued" limited the company's general obligation under the contract to compliance with the specific version of 29 CFR part 1926 in effect at the time bids were submitted. *Id.* The court agreed, finding that the contractual provision referring to the regulatory standard, though somewhat ambiguous, should be construed against the government as drafter of the contract. *Id.* at 516–17.

261. *See* Hughes Communications Galaxy, Inc. v. United States, 998 F.2d 953 (Fed. Cir. 1993).

262. *See* American Satellite Co. v. United States, 998 F.2d 950 (Fed. Cir. 1993).

263. *Hughes Communications Galaxy*, 998 F.2d at 955. According to the court, the government was promoting commercial use of its shuttle fleet by private industry to offset the costs of its space program. *Id.*

264. *Id.* at 956.

265. *See American Satellite Co. v. United States*, 26 Cl. Ct. 146 (Ct. Cl. 1992); *Hughes Communications Galaxy, Inc. v. United States*, 26 Cl. Ct. 123 (Ct. Cl. 1992).

266. *See American Satellite*, 26 Cl. Ct. at 158; *Hughes Communications*, 26 Cl. Ct. at 140, 145 (rights are subject to future policy changes).

on August 6, 1982.[267] While the court found that the government's promise satisfied the "unmistakability" standard,[268] there are reasons to doubt that the court was applying anything other than normal principles of contract interpretation to the launch service agreements. First, similar to *Winstar*, the court considered the unmistakability doctrine only after it had already determined that the government had breached the agreement by changing the launch policy.[269] Second, the court distinguished its holding from the Supreme Court's decisions in *Bowen* and *Merrion*, noting that in contrast to these cases, the plaintiffs did not actually seek to "enjoin the exercise of sovereign power" but rather claimed only monetary damages arising out of the government's breach.[270] On remand, the claims court considered and rejected several additional defenses raised by the government based on contractual provisions that allegedly limited the government's liability.[271] According to the claims court, none of the provisions overcame the government's contractual assumption of liability for future changes in launch policy.[272]

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267. *See American Satellite*, 998 F. 2d at 952; *Hughes Communications*, 998 F.2d at 957–58. Under the 1982 policy, the plaintiffs' commercial payloads were scheduled for launch. Under the new 1986 policy, the plaintiffs were advised that they would probably not be offered launch services. *Id.* at 957.

268. *See id.* at 958. The court stated:

> Under our interpretation of the contract, we have no trouble concluding that Article IV obligates the government to provide launch priority and scheduling in accordance with the August 6, 1982, policy in language which more than satisfies the "unmistakable terms" requirement. *Id.*

269. *See Hughes Communications*, 998 F.2d at 958.

270. *Id.* at 958–59.

271. *See* American Satellite Co. v. United States, 34 Fed. Cl. 468, 479 (Fed. Cl. 1995)

272. *Id.* at 479. The government first argued that it should not be held liable based on language in the contract which stated "All launch and associated services to be furnished by NASA to the Customer under this agreement shall be so furnished by NASA using its best efforts." *Id.* at 475. According to the government, NASA had used its "best efforts" but had been unable to provide launch services due to the 1986 policy change. The court rejected this argument for two reasons: 1) the contract allocated liability for such events (policy changes) to the government; and 2) NASA and the federal government are indistinguishable for purposes of government acts and thus the deliberate change in policy in 1986 undermined NASA's claim that it used its "best efforts" to provide services. *Id.* at 475–76. Second, the government argued that the 1986 policy change constituted a legal termination of the launch agreement due to language which allowed NASA to rescind the contract based "upon a determination in writing that NASA is required to terminate such services for Reasons Beyond NASA's Control." *Id.* at 476–77 (phrase Reasons Beyond NASA's Control is from the Launch Service Agreement). Such "reasons" were defined in the contract to include "acts of the United States Government other than NASA, in either its sovereign or contractual capacity." The government's straightforward argument was that the 1986 policy change was an act of the United States, beyond NASA's control. The court rejected this argument without much reasoning, noting only that policy changes subsequent to the execution of the contract cannot excuse the government from its contractual obligation to perform in

One might fairly argue that the satellite cases actually exemplify how the unmistakability standard should properly be applied to quasi-regulatory contracts; that where the government makes a specific promise to provide services according to a specific legal regime, the government should be held to its promise.[273] Another argument could be made that the launch agreement falls more squarely into the "market participant," rather than the "quasi-regulatory," model and thus the government could never have retained authority to simply "change" the terms of the contract.[274] However one views the court's decision, the court's application of the unmistakability presumption remains nevertheless suspect. The court discusses the unmistakability standard only as an afterthought to its contractual interpretation and then applies a pseudo-remedy test to alleviate any concerns that its treatment of the doctrine has been too cavalier.[275] By downplaying the proper interpretive role of the unmistakability doctrine, the court was able to find the government liable for a change in policy caused by an unforeseen emergency-like event,

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accordance with the 1982 policy. *Id.* at 478. Finally, the government argued that the plaintiffs had waived their right to bring a claim by agreeing to contract language which read " . . . the Customer shall not make any claim against the United States Government . . . for Damage or other relief . . . for the non-performance or improper performance of Launch and Associated Services . . ." *Id.* at 478. The government supported this argument by other contractual language showing that, in order to further space exploration and exploitation, both parties had agreed to forego recourse against one another in case of losses experienced by either side. The court chose to frame this issue as "whether [this provision] should be construed to apply when one party chooses not to honor the contract's obligations." *Id.* at 478-79. The court then held that the non-liability provisions only protected the government against "non-willful" breaches of contract, which would not include willful changes in policy regarding commercial launches. The court's ruling was influenced by its additional findings that the non-liability defenses only applied to "[c]ertain risks of [l]iability" arising out of "standard and optional shuttle Services such as launch and retrieval." The court interpreted these findings as meaning that the government was only "protecting itself against risks of failure associated with the "operational" aspects of the government's undertaking." *Id.* at 479-80.

273. As discussed above, this was the unmistakability standard adopted by Justice Scalia in *Winstar*. *See supra* notes 47-49 and accompanying text. *See infra* notes 294-306 and accompanying text for a discussion of an appropriate unmistakability standard.

274. This argument is bolstered by the court's language in *Hughes* that the government offered commercial launches in order to raise money for the space program. *See supra*, note 263. Under a market participant approach, the government would assert, under the sovereign acts doctrine, that the change in launch policy was a sovereign act, outside the control of the government acting in its contractual capacity. *See infra* notes 364-66. The court in *Hughes* rejected the government's sovereign act defense, however, on the grounds that the launch agreement shifted responsibility to the government for changes in policy. 998 F.2d at 958, n.8.

275. The remedy test applied by the *Hughes* court, though not precluding the application of the unmistakability doctrine, may be properly viewed as the precursor to the test ultimately adopted by Justice Souter in *Winstar*.

despite the presence of numerous contractual provisions purporting to limit the government's liability.[276]

A potential response to the demise of the unmistakability doctrine in federal contract takings jurisprudence is indifference. One might argue, in other words, that courts do not need the unmistakability presumption to find that limited liability provisions do in fact limit the government's liability[277] or that contractual rights under quasi-regulatory contracts are still subject to subsequent legislation.[278] This was essentially Justice Breyer's concurring argument in *Winstar;* that the government's authority to regulate for the general welfare can be adequately protected by "the law applicable to contracts between private individuals."[279] While this assertion may be debated, a larger question looms in regards to how courts will implement this obligation to protect the government's sovereign power. A comparison of the

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276. *See also* Conoco Inc. v. United States, 35 Fed. Cl. 309, 330-36 (1996). In *Conoco,* the court addressed whether subsequent statutes imposing additional obligations on lessees had breached off-shore oil and gas leases and taken the lessees' property rights arising out of the lease contracts. The court interpreted the terms of the underlying leases without applying the unmistakability doctrine. Instead, the court applied the doctrine only after finding the government had breached the agreement by imposing the additional obligations and delaying the approval of the lessees exploratory drilling proposals. In finding the unmistakability doctrine unhelpful to prevent government liability, the court stated:

> The terms of a government contract, *like any other contract,* do not change with the enactment of subsequent legislation absent a specific contractual provision providing for such a change. *Id.* at 336, quoting *Winstar Corp.,* 64 F.3d 1531, 1547 (Fed. Cir. 1995) (emphasis added).

The court's language is, of course, exactly opposite to the rule enunciated by the unmistakability doctrine, that government contracts are subject to subsequent exercises of sovereign power in the absence of unmistakable language to the contrary. *See supra* note 27.

277. *See, e.g,* O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995). In *O'Neill,* the 9th Circuit applied the unmistakability doctrine to find that federal water contracts were subject to the subsequent exercise of sovereign power by the government, and thus the government could not be found liable for failing to deliver the contract's full water allotment due to the implementation of sovereign acts, in this case the Central Valley Project Improvement Act, Pub. L. No. 102-575, 106 Stat. 4706-31 (1992). *Id.* at 682-86. Prior to reaching this holding, however, the court, applying normal principles of contract law, had already read a general provision in the contract that limited government's liability for shortages due to "any other causes" as precluding government liability. *Id.* at 684.

278. Justice Souter's opinion in *Winstar* characterized the Court's holding in *Bowen* as having read "the terms of a state-federal coverage agreement to reserve the Government's right to modify its terms by subsequent legislation . . . ." *Winstar,* 116 S. Ct. at 2456. Justice Souter's observation that the unmistakability doctrine was merely an "alternative" basis for the Court's decision in *Bowen* is not supported by the language of the opinion, which does not distinguish between the application of the unmistakability doctrine and a straightforward contractual reading. *See supra* notes 78-85 and accompanying text.

279. *Winstar,* 116 S. Ct. at 2473.

decisions in *O'Neill*,[280] *Peterson*,[281] *Hughes Communications*,[282] and *Conoco*,[283] as well as the numerous contradictory opinions (including *Winstar*) that have interpreted forbearance agreements affected by FIRREA,[284] hardly inspires confidence. These cases demonstrate that a rule of general contract interpretation does not result in decisions that transcend how individual judges feel about the relative benefits of government regulation and the respective equities of the contracting parties. The next section will discuss possible ways in which a greater consistency in federal contract interpretation may be achieved.

2. *Federal Contract Interpretation After* Winstar

This section presents a comprehensive framework in which courts may interpret rights and obligations under the wide variety of agreements entered into between the federal government and private parties. The purpose of this framework is to establish basic principles that lead to more consistent judicial decision-making while simultaneously striking an appropriate balance between the worthy societal goals of 1) preserving the government's regulatory authority and 2) protecting private parties from government actions that attempt to manipulate the potential advantages conferred by the unmistakability presumption. The *Winstar* opinion attempts to resolve the inherent tension between these goals through its formulation of the "remedy test," which eliminates the unmistakability doctrine from federal contract interpretation except in cases where a private party attempts to enjoin - or avoid - the operation of the sovereign power. As discussed extensively above, the remedy test, unsupported by law or precedent, ultimately fails to achieve its stated objective, to preserve the exercise of the government's sovereign authority.[285] The basic framework

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280. *O'Neill*, 50 F.3d at 686.

281. Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 808 (9th Cir. 1990).

282. Hughes Communication Galaxy, Inc. v. United States, 998 F.2d 953, 958 (Fed. Cir. 1993).

283. Conoco, Inc., 35 Fed. Cl. at 335-36.

284. *See, e.g.*, Winstar Corp. v. United States, 64 F.3d 1531, 1547 (Fed. Cir. 1995) (government made binding promise to provide favorable regulatory treatment in the future); Winstar Corp. v. United States, 994 F.2d 797, 813 (Fed. Cir. 1993) (government made no binding promise to provide favorable regulatory treatment in the future). *See also* Transohio Sav. Bank v. Director, Office of Thrift Supervision, 967 F.2d 598 (3d Cir. 1992); Carteret Sav. Bank, FA v. Office of Thrift Supervision, 963 F.2d 567 (3rd. Cir. 1992); Far West Fed. Bank v. Director, Office of Thrift Supervision, 951 F.2d 1093 (9th Cir. 1991); Guar. Fin. Servs. Inc. v. Ryan, 928 F.2d 994 (11th Cir. 1991); Franklin Fed. Sav. Bank v. Director, Office of Thrift Supervision, 927 F.2d 1332 (6th Cir. 1991). *See also* cases cited *supra* note 170.

285. In other words, in the real world of government agreements and regulation, the threat of monetary damages against the government is indistinguishable from the threat of

presented in this section rejects the remedy test in favor of a blanket presumption, applicable to all government contracts, that the government retains its sovereign powers unless surrendered in unmistakable terms. The next subsection will outline this framework. The subsection following will discuss the application of the basic framework principles to some of the recent cases, including *Winstar*.

a. Basic Framework For Interpreting Sovereign Power in Federal Contracts

The framework presented in this part is based on the recognized dual roles of the federal government as a sovereign authority and as a private contractor. These different roles are not set aside when the government enters in contractual arrangements.[286] Instead, the wide variety of government agreements reflect a similar range of government contractual capacities, from quasi-regulator to pure market participant.[287] The need to distinguish the quasi-regulatory and market participant models of government contracts from one another is brought into further focus when one examines the respective roles of the unmistakability and sovereign acts doctrines in interpreting government contracts. In short, the principles underlying the sovereign acts doctrine - that the government as contractor should be treated like any other private party - are not applicable to contracts falling within the quasi-regulatory model, in which the government enters into contracts more as a sovereign than as an ordinary market participant. Thus, a necessary first step in establishing a coherent analytical framework of federal contract interpretation is to distinguish between quasi-regulatory and market participant contracts.

For purposes of this framework, some basic principles may be used to distinguish between the two contractual types. First, is the contract part of an overarching regulatory scheme in which the government is using its contractual power to promote a specific public purpose, as opposed to the mere purchase of needed goods and services? Second, is the contract the type of agreement normally entered into by private parties or is the nature of the contract instead derived from the government's unique position as sovereign?[288] Third, was the contract formed through a standing contractual offer voluntarily accepted by the private party, without any bargained-for

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legislative enjoinment. In both instances, the effective exercise of sovereignty is blocked. *See supra* note 175.

286. *See, e.g.*, Schwartz, *supra* note 120 at 674-97; Griffith, *supra* note 120 at 305-16.

287. As Professor Schwartz notes, "[*Bowen*] suggests a distinction between conventional contracts that have private analogues . . . and uniquely governmental contracts that are integrally intertwined with a regulatory or social service program of the government . . . ." *See* Schwartz, *supra* note 120, at 686.

288. *See id.* at 686, 689.

consideration, or was the contract instead created through a more specific formation process, i.e. a competitive bidding procedure or individual negotiation.[289] While additional factors may aid a court in evaluating the nature of the government contract, the purpose of this framework is not to establish rigid boundaries of separation. Instead, a court should use these factors to gain insight into how the sovereign doctrines may be applied in interpreting rights under the underlying agreement.[290]

(1) Interpretation of Quasi-Regulatory Model Contracts

For purposes of this analysis, the important aspect of quasi-regulatory contracts is the essentially sovereign role played by the government in formulating and entering into the agreement with the private party.[291] As a result, the sovereign acts doctrine, which assumes the government acted in a purely contractual capacity when it entered into the agreement, does not readily apply. In the quasi-regulatory model, the fusion of the government's roles as contractor and legislator does not necessarily render the government liable for its sovereign acts,[292] as is the case under

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289. *See, e.g., Winstar Corp.*, 64 F.3d at 1546; *Winstar Corp. v. United States*, 25 Cl. Ct. 541, 545–46 (1992).

290. One may imagine, of course, particularly difficult cases, a few of which will be discussed below, where government contractual agreements seem to fall into both model categories simultaneously. In these cases, the best approach may be simply to apply both interpretive approaches; the different results should be sufficiently instructive to inform the decisionmaker as to how to proceed. *See infra* notes 355–70 and accompanying text.

291. A confusing aspect of this assertion are the many cases holding that the government acts in its "proprietary" rather than "sovereign" capacity when it enters into various agreements which this article would describe as quasi-regulatory. *See, e.g.*, Alabama v. Texas, 347 U.S. 272, 273 (1954) (in disposing of and administering the public lands, the United States acts in a "proprietary" role); *accord* United States v. Midwest Oil Co., 236 U.S. 459, 474 (1915). *See also* Sun Oil Co. v. United States, 572 F.2d 786, 818 (Ct. Cl. 1978) (United States acts in proprietary role when it enters into leases with private companies to explore for and develop offshore oil and gas resources); Utah Int'l, Inc. v. Andrus, 488 F. Supp. 962, 969 (C.D. Utah 1979) (BLM regulations defining commercial quantities test under the Mineral Lands Leasing Act constitute actions taken by sovereign in its proprietary, as opposed to regulatory, role). Generally, the purpose of the "proprietary-sovereign" distinction drawn in these cases is to show that rights arising out of such "proprietary" agreements are contractual in nature. *See, e.g., Sun Oil*, 572 F.2d at 818. Thus, these holdings do not ultimately conflict with the quasi-regulatory/market participant approach, which attempts to refine further the different models of government agreements that confer contractual rights on private parties.

292. For a different view, *see* Note, *Contracts – Financial Institutions Reform, Recovery, and Enforcement Act – Federal Circuit Holds Federal Government Liable for Breach of Thrift Contracts*, Winstar Corp. v. United States, 64 F.3d 1531 (Fed. Cir. 1995) (en banc), *cert. granted*, 116 S. Ct. 806 (1996), 109 Harv. L. Rev. 1162, 1167 (1996) (where government contracts in its sovereign capacity as a regulator or lawmaker, the government should be liable for direct breaches of the contract's terms). The problem with this approach is that it fails to take into

the market participant model. Instead, liability flows from the terms of the agreement and the authorizing statute, as set forth by the government as sovereign authority. It is in this interpretive context that the unmistakability doctrine plays a role, requiring a court to find that the quasi-regulatory agreement is subject to the sovereign's continuing authority to alter the contract's terms, pursuant to valid sovereign acts, unless the sovereign has waived that authority in unmistakable language.[293]

(a) Unmistakability Standard for Quasi-Regulatory Contracts

Case law provides a confusing array of factors and tests to determine whether the government has made a binding contractual promise.[294] To some degree, one may slice through this heavy precedent by

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account that contracts entered into by the government in its sovereign capacity are nevertheless subject to the exercise of future sovereign authority. *See, e.g., Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment*, 477 U.S. 41, 52 (1986). In fact, the argument is a classic example of the difficulties that arise when attempting to apply the principles of the sovereign acts doctrine to quasi-regulatory agreements.

293. *See* cases cited *supra* note 27.

294. In one category of decisions, courts find no unmistakable waiver on the grounds that express statutory reservations of sovereign power overcome the government's express promises to perform. *See, e.g., Bowen*, 477 U.S. at 53; National R.R. Passenger Corp. v. Atchison, Topeka & Santa Fe Ry. Co., 470 U.S. 451, 467–68, n.22 (1985); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 720 (1878). In a second, courts find no unmistakable waiver, even in the absence of an express statutory reservation, where the government's promise to perform is merely implied. United States v. Cherokee Nation of Okla., 480 U.S. 700, 707 (1987) (no express promise to surrender navigational easement in contract); Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 148 (1982) (no express promise to surrender taxation power in contract). *See also* Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 808 (9th Cir. 1990) (congressional failure to expressly reserve power to amend statute does not mean it unmistakably surrendered its power to do so); Manigault v. Springs, 199 U.S. 473, 480 (1905) (obligations under contract do not prevent government from exercising powers necessary for public good); Home Bldg. & Loan Ass'n. v. Blaisdell, 290 U.S. 398, 435 (1934) (reservation of essential attributes of sovereign power is read into contracts as a postulate of the legal order); Veix v. Sixth Ward Bldg. & Loan Ass'n, 310 U.S. 32, 38 (1940) (all contracts made subject to paramount authority to safeguard the vital interests of the people). A third group of cases finds waivers of sovereign power where the underlying contract or statute makes specific reference to a particular legal regime under which the contractual rights of the parties shall be determined. *Winstar*, 116 S. Ct. at 2450 (contractual provisions appear to lock in then-current regulatory treatment); American Satellite Co. v. United States, 998 F. 2d 950, 952 (Fed. Cir. 1993); Hughes Communications Galaxy, Inc. v. United States, 998 F.2d 953, 957 (Fed. Cir. 1993) (launch agreements commit government to provide launch services according to 1982 Presidential policy); Conoco Inc. v. United States, 35 Fed. Cl. 309, 335 (1996) (statute under which lease agreements executed subjects lease operations to specific existing laws). Among cases in this category, only Justice Scalia's opinion in *Winstar* and the satellite decisions (*Hughes* and *American Satellite*) characterize the government's waiver as "unmistakable." Finally, decisions within each of these categories place different degrees of emphasis on contractual provisions that attempt to limit the government's liability. *See, e.g.,*

observing that the waiver of the sovereign's implied right to alter the terms of a quasi-regulatory agreement is in essence simply a promise by the sovereign not to change the law that applies to the underlying contract.[295] What does such a promise look like? The key to this question begins with the recognition that not all government promises are equal. While some require the government simply to perform a contractual obligation, others go further, requiring the government to perform an obligation according to a specific set of legal parameters. In *Winstar*, for example, the thrifts argued successfully that the government promised to provide them a specific regulatory treatment, which was to take precedence over other regulations promulgated by the agencies.[296] In the satellite cases, the court found that the government had promised launch services according to specific policy set forth in a 1982 Presidential directive.[297] In *Conoco*, the court interpreted plaintiff's offshore lease agreements to incorporate only specifically enumerated future regulations.[298] Each of these promises related specifically

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O'Neill v. United States, 50 F.3d 667, 682–86 (9th Cir. 1995). *American Satellite*, 998 F. 2d at 952; *Hughes*, 998 F.2d at 957–58.

295. Some courts, without distinguishing between quasi-regulatory and market participant contracts, have characterized this promise as simply a contractual allocation of risk to the government for the possibility of future changes in the law. *See, e.g., Winstar*, 116 S. Ct. at 2460–61, 2476; *Hughes* 998 F.2d at 958–59. While both interpretations result in government liability, it is conceptually difficult to imagine that the government, contracting as a sovereign under the quasi-regulatory model, assumes a "risk" that its sovereign acts, over which it presumably *has* control, will cause damages to its contractual partner. *See infra* notes 335–38 and accompanying discussion regarding the unmistakability standard for the government in its role as contractor under the market participant model.

296. *Winstar*, 116 S. Ct. at 2450.

297. *American Satellite*, 998 F. 2d at 952; *Hughes*, 998 F.2d at 957–58.

298. *Conoco*, 35 Fed. Cl. at 322. In *Conoco*, the lease agreements were issued under the authority of the Outer Continental Shelf Lands Act, 43 U.S.C. §§ 1331–56 (1994). (OCSLA). Each lease agreement stated that it was issued pursuant to 1) OCSLA; 2) all regulations issued pursuant to OCSLA and in existence upon the Effective Date of the lease; 3) all regulations issued pursuant to OCSLA in the future which provide for the prevention of waste and conservation of the natural resources of the outer continental shelf and the protection of rights therein; and 4) all other applicable statutes and regulations. *Conoco*, 35 Cl. Ct. at 317. The government argued that the statutory amendments subsequently passed by Congress as part of the Outer Banks Protection Act of 1990, codified at 33 U.S.C. § 2753(c)(1), were incorporated into the terms of the lease by the "all other applicable statutes and regulations" lease language. *Id.* at 320–21. The court disagreed, observing that the drafters knew how to specify, and thus put the lessees on notice of, specific future legislation when they desired, as indicated by the lease language specifically subjecting the leases to future regulations issued pursuant to OCSLA for environmental protection. *Id.* at 322. The court then held that the general provision relating to all other applicable statutes did not include legislation enacted subsequent to the lease execution based on the general rule that "[w]here certain things are specified in detail in a contract, other [terms] of the same general character relating to the same matter are generally held to be excluded by implication." *Id.* (citing GROVER C. GRISMORE, PRINCIPLES OF THE LAW OF CONTRACTS, § 105, at 164, (1947)). In

to the sovereign authority alleged to have been surrendered.[299] In comparison, many other government promises, such as a promise to deliver a fixed amount of water or to charge a particular royalty rate on a renewable mining lease, make no mention of the sovereign power which authorize the promise in the first place.[300] In contrast to *Winstar*, in which the "very subject matter" of the contracts was regulation,[301] such express promises to perform do not by implication waive the government's right to exercise its reserved sovereign power.[302] As a result, ordinary governmental contractual promises, even when expressly stated, should not be considered an unmistakable waiver of sovereign authority.[303] Such a characterization defeats the purpose of the unmistakability doctrine, to prevent the *implied* waiver of governmental power.

In the absence of an unmistakable waiver, the quasi-regulatory contract remains subject to future exercises of the government's sovereign power. If the court finds an unmistakable waiver, however, a second question then arises whether such waiver is overcome by statutory or contractual language purporting to reserve the sovereign authority or otherwise limit the government's liability. While there is no simple answer to this question, one may reliably proceed according to the common law rule that specific contractual language supersedes more general provisions.[304] Thus, a government commitment to a specific legal regime

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making these rulings, the court never applied the unmistakability doctrine based on its holding that the doctrine's only role was to determine the availability of the sovereign acts defense. *Id.* at 339–40. *See supra* note 191 and accompanying text. Despite its erroneous failure to apply the doctrine (the case was decided before *Winstar*) the court's contractual interpretation is sound, illustrating how normal principles of contract interpretation may be used to determine whether a surrender of sovereign power was in fact unmistakable.

299. This approach is consistent with Justice Scalia's opinion that the unmistakability doctrine does not require that a contract explicitly waive Congress' power to legislate in the future in order to constitute an unmistakable surrender. *Winstar*, 116 S. Ct. at 2477; *See also* Statesman Sav. Holding Corp. v. United States, 26 Cl. Ct. 904, 921 (1992).

300. *See, e.g.*, O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995); Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780, 789 (D.C. Cir. 1990).

301. *Winstar*, 116 S. Ct. at 2476 (Scalia, J., concurring).

302. United States v. Cherokee Nation of Okla., 480 U.S. 700, 707 (1987) (court refuses to find implied contractual waiver of navigational easement); Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 148 (1982) (court refuses to find implied contractual waiver of taxation power).

303. Moreover, this conclusion should not depend on whether the authorizing statute expressly reserved the right of future amendment or repeal. *See, e.g.*, Peterson v. U.S. Dep't of Interior, 899 F.2d 799, 808 (1990) (no requirement that Congress expressly reserve the right to repeal, amend or alter legislation to preserve its fundamental right to do so); cases cited *supra* note 68.

304. *See* cases cited *supra*, note 255.

should take precedence over the general language of statutory reservation[305] or boilerplate provisions limiting the government's liability.[306] A more difficult question is presented when reservation or liability limitation language is also relatively specific. In such a case, it seems logical to conclude that, where waiver and reservation share a general level of specificity, the result is ambiguous and the alleged surrender of sovereign power clearly not "unmistakable."

(b) Interpretive Challenges under the Quasi-Regulatory Model

Unfortunately for practitioners, the interpretation of rights under federal contracts proves the rule that legal disputes involving actual parties are never as neat as the models formulated to solve them. Courts will, undoubtedly, face numerous challenges in applying the basic model to the actual interpretation of quasi-regulatory contracts. Most of these challenges center around two basic issues.

The first issue concerns the nature of the government act that effects the underlying contractual agreement. The quasi-regulatory model envisions such an act to be a sovereign legislative or regulatory enactment, which directly amends the statute and underlying agreement on which the private party's rights are based. Under this formula, the government act modifies the terms of the contract without "taking" property, since the private party does not possess any property interests existing outside federal sovereign authority. Western water law provides another example in this regard. In California, Central Valley Project water contracts are typically executed pursuant to the Reclamation Act and all amendatory or supplementing acts.[307] The 1992 Central Valley Project Improvement Act (CVPIA) amended the Reclamation Act to require, among other things, reductions in the amounts of fresh water diversions in order to enhance imperiled fish and wildlife populations.[308] Under the basic framework described above, these amendments should act directly on the terms of the contracts, modifying, for example, the amount of annual water delivery owed under the water contracts, according to the amended, controlling statute.

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305. This language typically reserves the right to "repeal, alter, or amend" the statute in question. *See* Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 53 (1986); National R.R. Passeng. Corp. v. Atchison, Topeka & Santa Fe Ry. Co., 470 U.S. 451, 467-68, n. 22 (1985); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 720 (1878).

306. American Satellite Co. v. United States, 998 F. 2d 950, 952 (1993); Hughes Communications Galaxy, Inc. v. United States, 998 F.2d 953, 957-58 (1993).

307. *See, e.g.*, O'Neill v. United States, 50 F.3d 677, 686 (9th Cir. 1995).

308. Central Valley Project Improvement Act, Pub. L. No. 102-575, 106 Stat. 4706-31 (1992).

A more difficult question is presented when sovereign actions affect the government's contractual obligations without specifically amending the underlying statutory. What happens, for example, if the same reductions in water deliveries are required instead under the Endangered Species Act (ESA),[309] a statute with no direct amendatory authority over the Reclamation Act. While the government would be similarly required to reduce water deliveries to its private contracting partners, it is unclear whether the ESA requirements would be properly characterized as having altered the terms of the underlying contract (and thus squarely within the quasi-regulatory model) or instead as having prevented the government from performing on its unmodified contractual obligation.

One approach to this question would be to assume that, as long as the amending statute was consistent with the purposes of the statute under which the quasi-regulatory contract was executed, the amendments should be incorporated into the contracts terms.[310] If instead the narrower standard (only direct amendments to the Reclamation Act may modify the underlying water contracts) were adopted, a second question arises: should a court allow the government to defend by asserting the sovereign acts doctrine, despite the *true* fiction that would be required to treat the Bureau of Reclamation, the administrator of the CVP water system, as just another private contracting party?[311] There are, of course, no easy answer to these questions. That does not mean, however, that the answers are not still important. If the government is required to defend its contractual nonperformance due to ESA mandated water reductions under the sovereign acts doctrine, it will be required to show that the listing of the endangered species was an unforeseen event, contrary to the assumptions of the parties at the time of contracting.[312] Given the growing awareness of the environmental impacts of water diversion on the Delta's ecosystem, however, this showing of unforeseeability may become increasingly difficult to make, particularly with regards to more recently executed water contracts.[313]

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309. 16 U.S.C. § 1531–44 (1994).

310. *Union Pac. R.R.*, 99 U.S. at 721 (the alterations must be reasonable and consistent with the object and scope of the authorizing statute). Note that such incorporation would be impermissible for contracts already executed, in which consideration had been exchanged. *Id.*

311. *See, e.g.*, Yankee Atomic Elec. Co. v. United States, 112 F.3d 1569, 1574–77 (Fed. Cir. 1997) (government may raise sovereign acts defense to claim that special cleanup assessment was actually a retroactive price increase on completed contracts for purchase of uranium).

312. *See supra* notes 99-112 and accompanying text; RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981) (impossibility defense).

313. The federal government has responded to this problem in two different ways. First, the CVPIA, which amends the Reclamation Act under which all water contracts are executed, specifically incorporates the water reduction requirements of the ESA into its terms. *See* 16

Another related question is what constitutes a "sovereign act" for purposes of the quasi-regulatory model? Under *Winstar*'s formulation of the sovereign acts doctrine, a sovereign act must be "public and general"[314] and not have the "substantial effect of releasing the government from its contractual obligations."[315] These parameters, designed for the market participant model, are less appropriate for quasi-regulatory agreements.[316] Instead, the limits on the government's sovereign authority must be found in the limits courts have always placed on government sovereignty, that is,

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U.S.C. § 3402(b)(2) (secretary required to dedicate and manage 800,000 acre-feet of CVP yield for various ecological purposes including meeting obligations as may be imposed under the Federal Endangered Species Act). This approach allows the government to argue that ESA mandated water reductions constitute de-facto amendments of Reclamation Act water contracts and thus do not give rise to a breach of contract on the part of the government requiring the sovereign acts defense.

The second approach has been to incorporate environmental requirements under the ESA and other related statutes directly into new water contracts as they come up for renewal. Negotiation between the Madera Irrigation District and the United States broke down over the government's insistence that the new contracts include the following language:

> The United States and the Contractor further agree that the provisions of this contract are subject to modification by the United States, after public meetings and discussions with the Contractor, . . . in accordance with the results of the final EIS and ESA consultation . . . and ESA and NEPA.

Madera Irrig. Dist. v. Hancock, 985 F.2d 1397, 1405 (9th Cir. 1993). The Ninth Circuit upheld the inclusion of these provisions by observing that "the government has not 'surrendered in unmistakable terms' its power to impose any environmental laws on the contractual relationship, so the required clause is not necessarily violative of Madera's contractual rights." *Id.* at 406. The court's reasoning illustrates how the government may inject external requirements from outside statutes (such as the ESA) into a quasi-regulatory agreement by inserting amendatory language that directly incorporates the statutory terms.

314. 116 S. Ct. at 2463 (citing Horowitz v. United States, 267 U.S. 458, 461 (1925)).

315. 116 S. Ct. at 2467.

316. *See supra* notes 185–94 and accompanying discussion. There are several reasons for this. First, regulatory enactments that effect quasi-regulatory contracts do not technically "release" the government from its contractual obligations; instead such obligations are already qualified by the government's retained authority of sovereign power. As is true for any regulation, subsequent legal changes may have a "substantial effect" on quasi-regulatory contracts, but this fact alone should not render the government actions invalid. Under the market participant model, a court may plausibly infer that a government act which substantially releases the government from its contractual obligations is more akin to a government action taken in its contractual capacity. The resulting fusion of the government's roles as contractor thereupon precludes the availability of the sovereign acts doctrine as an excuse for breach. Under the quasi-regulatory model, however, the fusion of the government's roles as a sovereign contractor and legislator is already assumed. Finally, the "public and general" requirement of the sovereign acts doctrine should not have any independent force, as applied to quasi-regulatory contracts, beyond emphasizing that the subsequent legal change must be pursuant to authorized statutory authority, that is, not selectively applied.

whether the legislation has a "legitimate public purpose."[317] The greater the impact of the legislation on the existing contract, the more scrutiny a court should apply in evaluating the reasonableness and necessity of the government's stated purpose.[318] Such heightened scrutiny has allowed courts, for example, to invalidate legislative actions which repudiate the government's financial obligations to its contractual partners without providing compensation.[319] The preference to "spend the money to promote the public good rather than the private welfare of its creditors" is, accordingly, not a sufficient public purpose justifying the severe impact to the government's contractual partners.[320]

The second issue around which interpretive challenges are sure to arise under the quasi-regulatory model is the nature of the impact to the private party's contractual rights. At the outset, it is clear that the measurement of a given "impact" on a contractual right due to government legislation is a tricky proposition. This is because such rights, in contrast to, say, a fee simple estate, may always be defined in terms sufficiently narrow to allege a complete extinguishment of an alleged property interest and thus a compensable taking under *Lucas*.[321] In *Bowen*, for example, the property interest alleged to have been taken was the narrow right to withdraw from the social security system, which right had been completely eliminated by Congress' amendment of the Social Security Act.[322] The elimination of the

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317. United States Trust Co. v. New Jersey, 431 U.S. 1, 22 (1977). *See also* Home Bldg. & Loan Ass'n v. Blaisdell, 290 U.S. 398, 438 (1934) (question is not whether the legislative action affects contracts directly or indirectly, "but whether the legislation is addressed to a legitimate end and the measures taken are reasonable and appropriate to that end."); Union Pac. R.R. Co. v. United States, 99 U.S. 700, 721 (1878) (legislative alterations must be reasonable and be made in good faith).

318. Energy Reserves Group v. Kansas Power & Light Co., 459 U.S. 400, 411 (1982); Allied Structural Steel Co. v. Spannaus, 438 U.S. 234, 245 (1977).

319. *United States Trust Co. v. New Jersey*, 431 U.S. at 29; *See also* Perry v. United States, 294 U.S. 330, 350-51 (1935); Norman v. Baltimore & Ohio R.R. Co., 294 U.S. 240, 304-05 (1935). For purposes of this article, these debt repudiation cases may also be distinguished from the quasi-regulatory model by the fact that the government, when it borrows money and contracts to repay it with interest, is not acting in a sovereign capacity. *United States Trust*, 431 U.S. at 25 n.23. Instead, these cases fall more squarely within the market participant model. *See infra* notes 355-63 and accompanying discussion.

320. *United States Trust Co. v. New Jersey*, 431 U.S. at 29. *See also* Lynch v. United States, 292 U.S. at 571, 580 (1934) (Congress does not have the power to repudiate its own debts simply in order to save money); Alpine Ridge Group v. Kemp, 955 F.2d 1382, 1386 (9th Cir. 1992); Yankee Atomic Elec. Co. v. United States, 33 Fed. Cl. 580, 585 (Fed. Cl. 1995) (legislation plainly directed at undoing a contractual liability previously assumed by the Government is an impermissible exercise of sovereign power).

321. Lucas v. South Carolina Coastal Council, 505 U.S. 1003, 1018-24 (1992).

322. Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 51 (1986). *See supra* notes 78-85 and accompanying text.

state's withdrawal right, however, did not terminate the state's overall participatory interests in the Social Security System, including the most important interest of all, the right to receive social security payments. As an analogy, one may consider the overall group of "rights" conferred upon a private party by a quasi-regulatory contract as similar to the "bundle of rights" contained within a fee simple estate. In this situation, each individual contractual right is analogous to the different "use interests" contained within the fee simple, many of which may be eliminated through valid exercises of the police power without violating the Fifth Amendment to the Constitution.[323]

This illustration is useful to show that the modification of many contractual rights - the right to pay a certain royalty amount[324] or the right to prepay on a government low income housing loan,[325] for example - may be considered to be something less than the complete extinguishment of a property interest. In the end, however, the approach one adopts in measuring contractual rights is not ultimately determinative. As discussed above, under the quasi-regulatory model the retention of sovereign authority means that validly enacted sovereign acts, reasonable and necessary for a legitimate public purpose, may completely extinguish a party's entire interest in the underlying contract without violating the Fifth Amendment.[326] Given this fact, an important question is whether there are any limitations on the government's ability to simply eliminate rights on which the private party has come to rely.

Some clues in answering this difficult interpretive question may be found in the oldest of the unmistakability decisions, *Sinking Fund Cases*, in which the Supreme Court characterized the reserved sovereign power as follows:

> [In amending the underlying contract, Congress] cannot undo what has already been done, and it cannot unmake contracts that have already been made, but it may provide for what shall be done in the future, and may direct what preparation shall be made for the due performance of contracts already entered into.[327]

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323. *Lucas*, 505 U.S. at 1016-19 and n.7; Penn Central Transp. Co. v. New York City, 438 U.S. 104, 123-24 (1978); *see also* Agins v. City of Tiburon, 447 U.S. 255 (1980); Keystone Bituminous Coal Ass'n v. DeBenedictis, 480 U.S. 470 (1987).

324. *Western Fuels v. Logan*, 895 F.2d 780, 789 (D.C. Cir. 1990).

325. Parkridge Investors Ltd. Partnership v. Farmers Home Admin., 13 F.3d 1192 (8th Cir. 1994).

326. *See supra* notes 248-50 and accompanying text.

327. Union Pac. R.R. Co. v. United States, 99 U.S. 700, 721 (1878).

Many of the quasi-regulatory unmistakability decisions fit well within this characterization. Typically such contracts - such as the social security agreements in *Bowen*, the water contracts in *O'Neil*, or the mining leases in *Western Fuels* - are of indefinite, or long, term with continuous exchanges of consideration between the parties. When Congress alters the terms of such agreements, it is providing "for what shall be done in the future" and directing "what preparation shall be made for the due performance of contracts already entered into," all reasonable exercises of the reserved power.[328]

A harder question is how to interpret the limitation that Congress cannot undo what has "already been done" or unmake "contracts that have already been made."[329] In *Bowen*, the Court holds at one point that the "conditional" nature of the state's alleged property interest is in part derived from the absence of any independent consideration paid by the state for the right to withdraw from the social security system.[330] *Bowen* thus appears to leave open the possibility that government's acceptance of independent consideration for the alleged contractual right may create a binding promise, even in the absence of an unmistakable waiver of sovereignty. The presence of independent consideration, however, merely begs the question of contractual intent; i.e. was the consideration provided to permanently bind the government to its stated promise, or rather to

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328. The Ninth Circuit's decision in *Madera Irrig. Dist. v. Hancock* is a good example of this principle. In *Madera*, the water users argued that an increase in water fees on renewable water contracts constituted an unconstitutionally retroactive alteration of property rights based on the allegation that the rates had been increased in order to recoup the prior subsidies provided by the federal government. 985 F.2d 1397, 1402-03 (9th Cir. 1993). In rejecting this claim, the court observed:

> Madera got its water during the forty year term and need pay no more for the old water than the price to which it agreed. Were it to buy no more water, it would owe no more money for the operations and maintenance expense .... The price of the new water will be calculated in such a way as to recoup a subsidy previously granted, as though the subsidy were a debt, but the subsidy is not owed like a debt. Madera has no obligation to repay it. *Id.* at 1403.

329. *See also* Bowen v. Public Agencies Opposed to Soc. Sec. Entrapment, 477 U.S. 41, 55 (1986) (Congress may not deprive a party of the fruits actually reduced to possession of contracts lawfully made) (citing Union Pac. R.R. Co. v. United States, 99 U.S. 700, 720 (1878)). One possible interpretation would be to characterize such language as an affirmation of Congress' ability to enter into binding regulatory contracts pursuant to an unmistakable waiver of its reserved sovereign powers. This was clearly not the approach intended by *Sinking Fund Cases*, which held that Congress had reserved its sovereign powers in executing the contracts. *Union Pac. R.R. Co.*, 99 U.S. at 719-20.

330. *Bowen*, 477 U.S. at 55. *See also* Alpine Ridge Group v. Kemp, 955 F.2d 1382, 1386 (9th Cir. 1992) (court distinguishes plaintiffs' claims from those in *Bowen* by finding that the plaintiffs have "bargained-for contract rights, supported by independent consideration."); *see also* cases, *supra* note 202.

preserve the benefits of the government's promise until such time that the promise was altered by a subsequent sovereign act?[331] If the consideration can be traced to a specific exchange of performance - royalties for mined coal or payments for water deliveries for example - then the performance received by the non-federal party may be legitimately characterized as vested property interests, immune from the effects of subsequent, retroactive legislation.[332] *Winstar* presents a slightly more complicated scenario, in which the consideration provides the government with the full benefit of the contractual bargain, while the government's performance obligation - in this case to provide favorable regulatory treatment - is ongoing. While the various opinions in *Winstar* do not elaborate on this point, it is clear the Justices in the majority were uneasy with simply allowing the government to withdraw its contractual promise after already

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331. As noted by Justice Rehnquist's dissent in *Winstar*, "[i]f the government agreed to let the losses acquired by [the thrifts] as supervisory goodwill in the short term, but made no commitment about their regulatory treatment over the long term, [the thrifts] still received consideration." 116 S. Ct. at 2484. The idea that consideration might be paid for such a conditional government commitment highlights the "temporal value" of such contractual rights, as discussed *supra* at notes 213-15 and accompanying text. A full discussion on the constitutionality of retroactive legislation is beyond the scope of this article. *See, e.g.*, Pension Benefit Guar. Corp. v. R. A. Gray & Co., 467 U.S. 717, 729-30 (1984) (retroactive application of a statute is constitutional if supported by a legitimate legislative purpose and furthered by rational means); Fisch, *supra* note 139.

332. *See* Yankee Atomic Elec. Co. v. United States, 33 Fed. Cl. 580, 586 (Fed. Cl. 1995), *rev'd on other grounds*, 112 F.3d 1569 (Fed. Cir. 1997). In *Yankee Atomic*, the Federal Claims court reviewed a congressional statute which authorized the Secretary of Energy to collect a special annual assessment from utility companies which had previously utilized enriched uranium, produced by the government, as a fuel in the operation of their nuclear plants. The purpose of the statute was to help defray the unforeseen cleanup costs of nuclear contamination. The utilities sued, claiming that the statute constituted an unlawful attempt to rewrite the terms of previously executed contracts in which the government had charged the utilities a fixed, per-unit price for its uranium enrichment services. 33 Fed. Cl. at 583-84. The court agreed, noting that "the assessment is an add-on to the price previously paid to the government" and that, "by imposing the assessment . . . the government dishonors the very promise it had earlier made: that the price to be charged for its services would not exceed the contract-stated maximum." *Id.* at 585.

The appellate court reversed, holding that the assessment statute was a general sovereign act that did not directly affect the completed contracts between the government and the utilities. The court noted that the language of the contracts did not preclude the government's sovereign authority to levy a general assessment for cleanup costs that were not considered at the time the contracts were entered into. Because the assessment did not alter the previously agreed upon price for enriched uranium, the government had not violated any contractual obligations. *See* 112 F.3d at 1574-80.

having received the full benefit of the contractual bargain, the bailout of the insolvent thrifts.[333]

(2) Interpretation of Market Participant Model Contracts

In the market participant model, the government enters into contracts, similar to any other private party, for the purchase and sale of products or services necessary to maintain the government's day to day operation. Thus, this model is perfectly suited for the sovereign acts doctrine, which assumes that the government's public and general sovereign acts are not attributable to the government as contractor.[334] The more interesting question under this model is the role the unmistakability doctrine plays, if any, in interpreting rights under market participant contracts. One might plausibly argue, for example, if the role of the government contractor under this model is analogous to a private market participant, why should the government be allowed *any* presumption that puts the government in a favorable position vis a vis its private contractual partner in determining liability under the federal contract?

The response to this argument may be stated simply. In market participant contracts, the unmistakability presumption merely ensures, in the absence of express language to the contrary, that the government shall be treated like any other private party in regards to sovereign acts which hinder or block contractual performance. When a court is asked to determine liability for contractual breach, the unmistakability presumption confers no advantage on the government in its fictitious role as a private party. Both parties may argue that they bear no responsibility for the occurrence of the sovereign act; the terms of the contract determine who prevails. The next two subsections will discuss the unmistakability standard and the mechanics of the sovereign defenses under the market participant model.

(a) Unmistakability Standard for Market Participant Contracts

The unmistakability standard for market participant contracts, while similar to the standard for quasi-regulatory contracts described above, differs in concept due to the distinct roles played by the government under the different contractual models. When the government contracts in its role as a sovereign under the quasi-regulatory model, its waiver of sovereign authority takes the form of a promise not to change the law.[335]

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333. In this respect, *Winstar* is probably a good model for government practitioners regarding the probable hostility with which the judiciary will greet quasi-regulatory agreements that do not in some way protect private party reliance on government promises that are subsequently withdrawn through the exercise of sovereign power.

334. *See supra* notes 95–108 and accompanying discussion.

335. *See supra* note 295 and accompanying discussion.

When the government contracts in its role as market participant, its waiver of sovereign authority takes the form of a promise to assume contractual responsibility for its acts as a sovereign, over which it presumably has no control. As is true under the quasi-regulatory model, if the government confers contractual rights on a party according to a specific legal regime, the government will be liable for sovereign acts which alter that legal regime and consequentially hinder or block contractual performance.[336] Under the market participant model, however, such liability derives not from the government's breach of its promise to maintain a certain legal regime, but instead as a result of the government's assumption of risk for legal acts of the sovereign beyond the control of the government in its contractual capacity.[337]

In the absence of an unmistakable waiver of sovereign authority, the government as market participant may of course simply assume liability for the *effects* of random sovereign acts, such as rises in the price of supplier goods or delays in delivery. Unlike a general waiver, however, such contractual assumptions of risk need not be unmistakable. Instead, courts will interpret such provisions as they would any other risk allocations negotiated between two private parties.[338]

(b) Mechanics of Sovereign Defenses under Market Participant Model

Upon reflection, it becomes clear that the role of the unmistakability doctrine in interpreting routine "market participant" contracts does not confer any advantage to the government. A judicial finding that the government did not waive its sovereign authority merely allows the government to raise the sovereign acts doctrine and have its contractual

336. *See supra*, notes 294-306 and accompanying discussion. The government might also unmistakably waive its sovereign authority through straightforward provisions allocating liability to the government for sovereign acts that hinder or block performance. Note that the government might arguably make an unmistakable promise not to alter the specific legal regime governing a particular contract, while at the same time making no such promises as to general sovereign acts that do not directly affect the contract terms. *See, e.g., Yankee Atomic*, 112 F.3d at 1580 (unmistakable promise not to change price of uranium was not unmistakable promise against a future assessment for cleanup costs).

337. This conclusion implies that the Justices in *Winstar*, in finding that the government had "assumed the risk of future regulatory change," were treating the forbearance agreements as "market participant," as opposed to "quasi-regulatory" agreements. *Winstar*, 116 S. Ct. at 2457-58.

338. Under the second requirement of the impossibility defense, for example, a court must examine the contract to establish whether its language or circumstances indicate that the parties actually allocated the risk of the alleged unforeseen event. *Winstar*, 116 S. Ct. at 2473; RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981); *see supra* note 35.

obligations adjudicated in the same manner as a private party.[339] While conferring no advantage, however, the application of the unmistakability doctrine to market participant contracts serves a valuable role in retaining the government's latitude to enact sovereign laws for the general welfare. This is particularly true where the sovereign act hinders or blocks the performance of the private contracting party.[340] In these situations, the unmistakability doctrine prevents the government from assuming responsibility, absent clear and express contractual language, for damages caused by the sovereign act.[341] In this respect, it should be noted that most government purchase and sale contracts, in fact, do allocate these types of risks with such express provisions.[342] Thus, the concern of the *Winstar* justices, that the application of the unmistakability doctrine to "routine supply contracts" would result in "compromising the government's practical capacity to make contracts," seems unjustified.[343]

A different concern is the appropriateness of *Winstar*'s test for determining whether a sovereign act is sufficiently "public and general" to

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339. *See* Jones v. United States, 1 Ct. Cl. 383, 384 (1865) (in this court the United States appear simply as contractors; and they are to be held liable only within the same limits that any other defendant would be in any other court).

340. Where the public and general sovereign act prevents the government's contractual performance, the unmistakability presumption is only marginally important; in these cases the government must still show that the occurrence of the act was unforeseeable and not otherwise allocated as a risk under the terms of the contract. RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981). Both of these inquiries will be conducted under normal contract principles of interpretation.

341. *Hills Materials Co. v. Rice* illustrates how a court's failure to apply the unmistakability doctrine to a market participant contract may result in government liability. Hills Materials Co. v. Rice, 982 F.2d 514 (Fed. Cir. 1992). In *Hills*, the court interpreted ambiguous provisions against the government, as drafter of the contract, in finding the government responsible for cost overruns experienced by the private contractor as a result of government regulations. 982 F.2d at 516–17. The court then rejected the government's sovereign acts defense on the grounds that the government had affirmatively assumed responsibility for the acts, despite the fact that the contractual risk allocation was susceptible to different interpretations and thus hardly "unmistakable." *Id.* at 516 n.2.

342. *See, e.g.*, 48 C.F.R. § 249.110 (1997) (prescribing provisions which may be inserted into government contracts in order to allocate risk in the event the government terminates performance of work). *See also* G. L. Christian & Assocs. v. United States, 312 F.2d 418, 423–24 (Ct. Cl. 1963); Schwartz, *supra* note 120 at 694–97; Spiedel, *supra* note 108 at 520–25.

343. *Winstar*, 116 S. Ct. at 2459. Justice Souter's concern regarding the effect of the unmistakability doctrine on the government's ability to enter into routine contracts appears to stem from the opinion's failure to make a distinction between the doctrine's application to market participant, as compared to quasi-regulatory, agreements. In other words, under Souter's approach, the application of the unmistakability doctrine to market participant contracts would allow the government to change the contract's terms, similar to the quasi-regulatory model, instead of simply allowing the government to raise the sovereign acts doctrine as a defense. *See supra* notes 59–145 and accompanying text.

warrant application of the sovereign acts doctrine.[344] According to Justice Souter, an act will not be considered "public and general" if it "has the substantial effect of releasing the Government from its contractual obligations...."[345] The "substantial effect" test asks whether the government's act has a direct impact upon the government's contract obligations or whether the impact is instead indirect or merely incidental to the accomplishment of other legitimate sovereign purposes.[346] While the test has been justly criticized for being difficult to apply, and for inviting inevitable inquiries into legislative intent,[347] the question remains whether the test is necessary to prevent the government from gaining unfair advantage under certain contractual scenarios. In some cases, where the government is still required to meet the requirements of commercial impossibility to avoid liability, the substantial effects test is arguably unnecessary.[348] In *Winstar*, for example, Justice Souter's finding that FIRREA had a direct, substantial effect on the government's contractual obligations[349] was largely superfluous since the contracts' treatment of the applicable regulations prevented the government from successfully arguing that the change in law was unforeseeable nor addressed by the contracts' terms.[350]

One may imagine, however, how the absence of a substantial effects test might in other situations allow the government to avoid appropriate responsibility for the effects of its sovereign actions. This possibility is particularly high where the sovereign act hinders or prevents the performance of the private party; in that case the government will be under

344. *See, e.g., The Supreme Court – Leading Cases*, 110 HARV. L. REV. 345 (1996).

345. *Winstar*, 116 S. Ct. at 2467.

346. *Id.* at 2466-67.

347. *The Supreme Court-Leading Cases, supra* note 344 at 353-54. *Winstar*, 116 S. Ct. at 2482-83 (Rehnquist, J., dissenting).

348. *See The Supreme Court-Leading Cases, supra* note 344 at 353-54.

349. FIRREA was arguably a "public and general" sovereign act, since it applied to the entire savings and loan industry and was passed in order to stave off an even more serious, predicted financial crises. Fin. Insts. Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, 103 Stat. 183 (codified as amended in scattered sections of U.S.C.). *See, e.g, Winstar*, 116 S. Ct. at 2483 (Rehnquist, J., dissenting) ("FIRREA made enormous changes in the structure of federal thrift regulation."). FIRREA was entitled "an act to reform, recapitalize, and consolidate the Federal deposit insurance system, to enhance the regulatory and enforcement powers of federal financial institutions regulatory agencies and for other purposes." *Winstar*, 116 S. Ct. at 2483 (Rehnquist, J., dissenting, quoting FIRREA, 103 Stat. 183 (1989)). The stated purpose of FIRREA is, in part, to provide affordable housing mortgage finance and housing opportunities for low and moderate income individuals by restoring the viability of the thrift industry. Toscano, *supra*, note 9 at 470.

350. *Winstar*, 116 S. Ct. at 2469-72. RESTATEMENT (SECOND) OF CONTRACTS, § 261 (1981).

no requirement to meet the impossibility standards.[351] Instead, the foreseeability of the "public and general" act will prevent the private party from having *its* performance excused, thus rendering it responsible for any resulting damages.[352] It is true, of course, that the real possibility of such occurrences is alleviated significantly by the ability of the parties to allocate such contractual risks through standard clauses and provisions.[353] For this reason, and because of the real shortcomings in implementation, as referred to above,[354] the significant effects test is probably not ultimately appropriate as a factor for determining the availability of the sovereign acts defense.

b. Application of Basic Framework Principles

The purpose of the basic framework is to set forth models of analysis from which courts may choose when addressing the government's sovereign defenses in federal contract interpretation. For many contracts, the most difficult call is whether the agreement falls within the quasi-regulatory or market participant model of analysis. In some respects, a court's determination of *which* model is not as important as the consistency of analysis once a model is chosen. The most directed criticism of recent court decisions involving the government's sovereign defenses is usually attributable to the failure to distinguish between regulatory and market models of government contracts. Where a government contract falls in the gray zone, somewhere between quasi-regulatory and market participant, a court is probably best advised to apply both models in interpreting underlying rights and obligations. Only where the different models produce opposite results will a court be forced to make a binding determination as to the nature of the underlying contract.

A short run through some of the more confusing "sovereignty" cases illustrates this principle. Two early Supreme Court decisions, *Perry v. United States*[355] and *Lynch v. United States*,[356] have continuously challenged those attempting to establish the boundaries of retained federal

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351. *See, e.g.*, Jones v. United States, 1 Ct. Cl. 383, 384 (1865) (government has no responsibility for sovereign act that increases cost of performance for private party); Deming v. United States, 1 Ct. Cl. 190 (1865).

352. *See* Tony Downs Foods Co. v. United States, 530 F.2d 367, 372 (Ct. Cl. 1976). In *Tony Downs*, a poultry supplier sued to recover increased costs it had incurred as a result of the government's termination of the national price freeze for certain products. The court first held that the government bore no responsibility for the price freeze, which the court characterized as "an exercise of sovereign power." *Id.* The court then rejected the poultry supplier's impossibility defense based on its finding that the lifting of price controls "cannot legitimately be viewed as unforeseeable or beyond reasonable anticipation." *Id.*

353. *See supra* note 342.

354. *See supra* note 347.

355. Perry v. United States, 294 U.S. 330 (1935).

356. Lynch v. United States, 292 U.S. 571 (1934).

sovereignty.[357] In *Perry*, the Court held that the government's refusal to pay bondholders in gold according to the terms of the bond notes was an impermissible repudiation of the government's obligation to honor its own debts.[358] *Perry*'s holding was in part based on *Lynch*, in which the Court held that Congress could not simply repeal its contractual obligations to pay benefits under the government's War Risk Insurance program.[359] While neither *Perry* nor *Lynch* fall comfortably within either of the two contractual models discussed,[360] analysis under either model conforms to the Court's ultimate decisions. Under the quasi-regulatory model, a court would likely find that the government's preference to relieve its own financial obligations was not a sufficiently valid public purpose to warrant the significant impact on the parties' right to receive payments according to the contracts' terms.[361] Under the market participant model, a court would likely hold that the government's role as contractor was not sufficiently distinct from its role in enacting the repealing legislation, thus precluding the assertion of the sovereign acts defense.[362] In *Perry*, one could additionally argue that the

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357. *See, e.g.*, Schwartz, *supra* note 120 at 675–83. Toscano, *supra* note 9 at 455-58; K. McKay Worthington, Note, *Is your government contract worth the paper its written on? An examination of Winstar v. United States*, 1 Columbia Bus. L. Rev. 119, 125–29 (1996).

358. *Perry*, 294 U.S. at 349–54.

359. *Lynch*, 292 U.S. at 577–78.

360. *Perry* arguably falls within the market participant model based on the language of *United States Trust*, which states that the government does not act as a sovereign when it borrows money and contracts to repay it with interest. United States Trust Co. of New York v. New Jersey, 431 U.S. 1, 25 n.23 (1977), *citing* Murray v. Charleston, 96 U.S. 432, 445 (1878). Conversely, *Lynch* falls more within the quasi-regulatory model due to the overarching public purpose and regulatory-like structure of the War Risk Insurance program.

361. *United States Trust*, 431 U.S. at 29. This was essentially the holding in *Lynch*, in which the Court noted that "the due process clause prohibits the United States from annulling [] [the policies or contracts] unless indeed, the action taken falls within the federal police power or some other paramount power." *Lynch*, 292 U.S. at 579. Note that the serious impact to the government's contracting partners as a result of the government's actions may heighten the scrutiny a court will apply to the government's alleged public purpose. Energy Reserves Group, Inc. v. Kansas Power & Light Co., 459 U.S. 400, 411 (1982); Allied Structural Steel Co. v. Spannus, 438 U.S. 234, 245 (1977). One might also argue in *Perry* that the government's obligation to repay the bond "in United States gold coin of the *present standard of value*," constituted an unmistakable waiver of its sovereign authority to change the terms of payment. *Perry*, 294 U.S. at 348 (emphasis added) (the term "present standard of value" establishes a standard of the government's obligation in contrast to any purported performance that amounts to a "lower standard of value"). In *Lynch* there was no arguable waiver, save for the payment of independent consideration through monetary premiums. *Lynch*, 292 U.S. at 577 (insurance policy subject to all amendments to original act).

362. This holding could be made on the grounds that 1) the government legislation had direct, significant effects on the government's contractual obligations; or 2) the government's repeal of its bond and insurance obligations were not public and general acts, but instead acts aimed clearly at specific government contracts. The fact that one could make a credible argument that the government repeals were in fact "public and general" acts illustrates the

government's specific promise to pay in gold was either an unmistakable allocation of liability for any change in the gold standard or, at the least, an indication that the parties had contemplated the possibility of such a change, thus precluding a defense based on impossibility.[363]

The satellite cases,[364] which also involve contracts arguably fitting under either model, further illustrate the convergence of result under the two distinct analytical approaches. A court might, for example, characterize the launch agreements as quasi-regulatory contracts entered into for the purpose of regulating commercial space activities. Under this model, the court could characterize the government's promise to provide launch services specifically according to 1982 policy as an unmistakable waiver of its right as sovereign to alter the terms of the agreement. Conversely, the Court could characterize the agreement as essentially market driven, and interpret the government's promise as an express assumption of contractual liability for actions of the sovereign that change launch policy.[365] Note that under this approach, sovereign actions that did not explicitly alter launch policy but still acted to block government performance on the contract - for example, the government's closure of the launch site due to an impending hurricane - might excuse the government's non-performance, notwithstanding the explicit waiver contained in the contract.[366]

The forbearance agreements in *Winstar* are also illustrative of contracts that fall near the mid-point of the regulatory-market spectrum. The agreements were not contracts that might have been entered into between private parties; instead they conferred specialized legal treatment on the thrifts as part of an overall regulatory approach to save the savings and loan industry from bankruptcy. On the other hand, the agreements represented bargained-for exchanges of consideration motivated primarily by the government's desire to avoid the potentially enormous expenses that could result from the insurance commitments of the FSLIC. The ambiguous nature of these contractual arrangements is clearly one cause of the inconsistent reasoning behind the court decisions that interpreted them.[367]

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potential importance of the "substantial effects" test in preventing the government from exploiting its rights under the sovereign acts doctrine. *See supra* notes 344-354 and accompanying text.

363. *Winstar*, 116 S. Ct. 2432, 2471-72. RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981).

364. *See supra* notes 260-76 and accompanying discussion.

365. This is probably the better model of analysis, given the court's observation that the commercial launch program was implemented as a way to offset the costs of the space program. Hughes Communications Galaxy, Inc. v. United States, 998 F.2d 953, 955 (Fed. Cir. 1993).

366. This result might also be theoretically possible under the quasi-regulatory model. *See supra* notes 309-12 and accompanying text.

367. *See* cases cited *supra* note 170.

As is true with the cases described above, however, the result reached by the Court in *Winstar*, that the government is liable for the damages caused to the thrifts due to the change in regulatory policy, may be arrived at under either model of analysis.[368] Under the quasi-regulatory model, the government's promise of specific legal accounting treatment may be treated as an unmistakable promise by the sovereign not to change the law. Under the market-participant model, the government's promise can be characterized as an unmistakable assumption of risk by the government should the legal framework be changed by the sovereign. In this model, the unmistakable waiver means that the government has waived its right to raise the sovereign acts doctrine as an excuse for breach. If Justice Souter's opinion were to be characterized as having found such an unmistakable risk allocation, *Winstar* should not have even addressed the government's sovereign acts defense.[369] Of course, Souter's opinion never identifies the government promise as "unmistakable," and thus, to the extent the forbearance agreements are considered to be market-participant contracts, the Court is correct in addressing the sovereign acts doctrine. Souter's opinion demonstrates, in fact, how a contractual allocation may not be "unmistakable" for purposes of deciding whether the government has waived its right to raise the sovereign acts defense, but still be sufficiently clear to preclude the government from avoiding liability once it is treated as just another private party under common law principles of contract interpretation.[370]

CONCLUSION

The government's sovereign defenses derive from historical lines of analysis which correspond to two different traditional government roles, one as sovereign regulator and the other as market participant. To make sense of the precedent standing behind the sovereign doctrines (and to apply the doctrines today in a coherent framework), it is thus necessary to interpret federal contracts under distinct analytical models that represent these two different governmental roles.

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368. One may of course quibble with the Court's factual and legal interpretations as to whether the contracts contained unmistakable promises which bound the government. The purpose in this paragraph is to show how an analysis might flow given different findings.

369. This was the approach recommended by Justice Scalia. *Winstar*, 116 S. Ct. at 2477 (Scalia, J., concurring) (sovereign acts doctrine is avoided whenever government makes an unmistakable promise that none of its sovereign acts will incidentally disable it or the other party from performing one of the promised acts).

370. *Winstar*, 116 S. Ct. at 2463-72. RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981) *See supra* notes 338–40 and accompanying text.

The unmistakability doctrine holds that the government will not be presumed to have waived its sovereign authority to make laws and regulations when it enters into contracts with private parties. When the government enters into "quasi-regulatory" contracts, the unmistakability doctrine retains the government's authority to alter the terms of future contractual performance, absent an express government promise to be bound by a specific legal regime. When the government enters into "market-participant" contracts, the unmistakability doctrine similarly retains the government's right to deny legal responsibility for public and general sovereign acts, absent express contractual language which assumes such liability.

Under the sovereign acts doctrine, the government is treated as a private party in determining liability for the effects of public and general sovereign acts which hinder or block contractual performance. Because the purpose of the sovereign acts doctrine is to allow the government to assert defenses, such as commercial impossibility, that would be available to a private party, the doctrine is well suited for interpreting liability under market participant contracts, in which the government contracts in a quasi-private capacity. For the same reason, however, the sovereign acts doctrine is not appropriate for determining rights under quasi-regulatory contracts, in which the government acts in an essentially sovereign capacity, entering into contractual arrangements in order to promote a greater regulatory objective. Instead, courts determine rights under these contracts by asking whether the alleged property interest is "subject to" or instead "vested" against the implied reservation of sovereign authority.

The *Winstar* decision fails to distinguish between the regulatory and market models of government contracts. Instead, Justice Souter's opinion relies on a less meaningful distinction, which limits the presumption of reserved sovereign authority to claims that effectively block, or exempt a party from the operation of, the government's exercise of sovereign power. While this article has pointed out many problems with the "remedy test," one stands out above all the others; the remedy test does not preserve the presumption of retained sovereignty in exactly those quasi-regulatory agreements for which the presumption is most appropriate. This conclusion is confirmed by considering the mechanics of a takings claim, the preferred remedy under quasi-regulatory contract right disputes. In a takings action, the party specifically does not seek to enjoin the government's right of eminent domain, a reserved, inalienable power under 19th century contract clause cases. Instead, takings claims seek just compensation, a pure damage remedy which, under the remedy test, will never require the invocation of the unmistakability presumption.

The different *Winstar* opinions also blur the relationship between the unmistakability and sovereign act doctrines, implying in parts of the decision that the unmistakability presumption merely serves to retain the

government's right to disclaim responsibility for its own sovereign acts. Like the adoption of the remedy test, this doctrinal merging has the effect of eliminating the unmistakability presumption from the interpretation of quasi-regulatory contracts. Such a shift in federal contract law has serious adverse consequences for the government's ability to regulate the activities of its contractual partners without running afoul of the Fifth Amendment's takings prohibitions. Unhappily, *Winstar* neither acknowledges nor discusses the implications of such a shift. If such a contraction of federal regulatory power is indeed warranted, *Winstar* does not tell us why that should be so.

In addition to identifying some consequences of *Winstar*'s precedent on federal contract interpretation, this article has set forth a basic framework in which courts should interpret rights and obligations under government contracts. The framework does not guarantee specific results. As always in contract interpretation, ultimate decisions on the merits, particularly in hard borderline cases such as *Winstar*, will be left to the fact finder. The framework has the potential, nevertheless, to establish consistent rules of interpretation which may be applied to the different contractual models. Consistent interpretation, a relatively rare commodity in recent decisions involving the government's sovereign defenses, allows parties to draft contractual provisions with greater certainty and to enter into the reliable binding commitments at times necessary to effectuate the public purpose of the regulatory contract.[371] Unfortunately, *Winstar* achieves quite the opposite result, setting forth a divergent set of opinions based on confusing and at times contradictory analysis. For this reason, *Winstar* deserves to be overhauled, as quickly as the next federal contract interpretation case can reach our nation's highest court.

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371. An example of how the need for binding government commitments in the regulatory field may create new government contract policy is provided by the "No Surprises" Statement adopted by the U.S. Fish and Wildlife Service and the National Marine Fisheries Service in regards to Habitat Conservation Plans under the Endangered Species Act. H.R. Rep. No. 97-835. The Statement provides that Habitat Conservation Plans entered into pursuant to 16 U.S.C. § 1533 may not be subsequently modified by the government except at the government's own expense. The impetus of the Statement is the political realization that "the major benefit from the HCP process from the perspective of the development community or land manager is *certainty*." (emphasis added). The stated purpose of the policy is to "provide assurances to non-federal landowners ... that no additional land restrictions or financial compensation will be required from an HCP permittee for species adequately covered by a properly functioning HCP in light of unforeseen or extraordinary circumstances."