

Comparative Constitutional Protection of Contracts in the United States and Chile

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Introduction

The purpose of this article is to highlight both the historical and the current symmetry between the legal foundations of the American doctrine of the “impairment of contracts,” and the principle of *intangibilidad de los contratos* (inviolability of contracts) under Chilean law.

This article advances the thesis that even though they proceed from two different juridical traditions, the American from the common law tradition, and the Chilean from the Roman-Canon-civil law traditions, both the American and Chilean systems share important similarities in jurisprudential developments regarding the protection of the sanctity of contracts, and by extension in the protection of the right to private property.

Accordingly, the authors undertook research into the legal foundations of the right to contract, focusing on the most significant decisions issued by both the United States and Chilean Supreme Courts. Thus, the authors’ research presents the law from a predominantly “active” and “practical” viewpoint that is, focused on

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jurisprudential developments. Consequently, the article includes an examination of the fundamental economic bases over which the constitutional and legal superstructure for the protection of contracts and private property has been built in both systems over the past two centuries. Equally important, the article aims at identifying the most controversial topics arising during this period.

In sum, this article advances the thesis that both legal systems have built the essentials of their contractual protection regimes based upon noticeably congruent legal and economic principles and policies, all of which ultimately can be derived from traditional Natural Law.

1. Setting the Framework: The Texts of the Constitutions

1.1. Origin of the United States “Impairment of Contracts” Doctrine

In the period between the United States War of Independence and the 1787 Constitutional Convention, there was a considerable impetus for the repudiation of the public and private debts from the period preceding the definitive peace of 1783. This desire was especially strong due to the post-war inflation,³ and was found mainly at the state level through the “discharge of previous contracts in an almost worthless currency[.]”⁴ and by the issuance and circulation of newly-coined money. Debtors took advantage of this situation, and successfully pressured state legislatures to pass emergency statutes suspending contracts and cancelling debts. Herein lies a fissure dividing the country after its independence and which operated, remotely, as one of the causes for the Civil War in the mid-nineteenth century.

On the one hand, creditors favored a strong central government to protect the sanctity of contracts. On the other hand, debtors championed a decentralization model that would

³ KERMIT L. HALL, *LAW, ECONOMY, AND THE POWER OF CONTRACT. MAJOR HISTORICAL INTERPRETATIONS* 512 (1987).

⁴ HENRY CAMPBELL BLACK, *HANDBOOK OF AMERICAN CONSTITUTIONAL LAW* 708 (1927).

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allow states to tolerate debt. Consequently, the former advanced a strong federal judicial system to defend private initiative, private property, and the development of corporations, while the latter promoted state legislative supremacy, with a more redistributive aim.⁵ Given the fact that the United States Constitution did not address the topic of contracts in detail, it was left to the United States Supreme Court to develop a coherent doctrinal framework for contract protection. This task was diligently tackled by Justices John Marshall and Joseph Story, who at the turn of the nineteenth century developed a jurisprudence setting forth the bases for the constitutional protection of contracts.⁶

A precursor to the establishment of the constitutional language protecting contracts is found in James Madison's Federalist Number 44:

... laws impairing the obligation of contracts, are contrary to the first principles of the social compact and to every principle of sound legislation [and are] prohibited by the spirit and scope of these fundamental charters [and, moreover, first principles are a] constitutional bulwark in favor of personal security and private rights[.]⁷

James Wilson⁸ is said to have been the remote author of the so-called "Contract Clause" of the Constitution when he argued in 1785 that, "whenever the state passes a law granting land, or granting charters of incorporation or other privileges ... such laws are to be considered as compacts."⁹ Now, during the discussions leading to the passing of the Contract Clause, according to Madison's notes, Rufus King,

a Massachusetts representative to the Constitutional Convention, proposed additional language to the Ordinance of Congress of 1787—which established the Northwest Territory— forbidding states "to interfere in private contracts."¹⁰ The definitive language adopted by the said draft Ordinance, which was supported by Madison, stated, "And in the just preservation of rights and property...no law ought ever to be made or have force in the said territory, that shall, in any manner whatever, interfere with or affect private contracts, or engagements, bona fide, and without fraud previously formed."¹¹

This proposal was judged to go too far and a motion emerged to replace it with a reference to "retrospective" (that is, "retroactive") laws instead.¹² The draft of the Constitution later contained a reference to "laws *altering* or impairing the obligation of contracts."¹³ However, there is no record as to the debates leading to the dropping of the word "altering" from the definitive text of the Constitution,¹⁴ which reads as follows:

Article I, section 10: "No State shall ... pass any ... Law impairing the Obligation of Contracts[.]"¹⁵

The Contract Clause was thus conceived of as a reinforcement of the rights of the people vis-à-vis governmental intrusion. Specifically, the rights, privileges, and "franchises"¹⁶ recognized by the federal and state governments were

5 JAMES WILLARD HURST, *THE GROWTH OF AMERICAN LAW: THE LAWMAKERS* 12 (1950).

6 HALL, *supra* note 3, at 513.

7 Cited in WARREN B. HUNTING, *THE OBLIGATION OF CONTRACTS CLAUSE OF THE UNITED STATES CONSTITUTION* 112 (1919).

8 *Id.* at 89 (stating that James Wilson "was considered one of the most learned members of the Constitutional Convention, and was later a member of the Supreme Court of the United States.").

9 *Id.* at 36-37.

10 Horace H. Hagan, *Fletcher vs. Peck*, 16 GEO. L. J. 1, 35 (1927).

11 *Id.* at 36.

12 *Id.* at 36.

13 *Id.* at 37 (emphasis added).

14 *Id.*

15 U.S. CONST. art. I, §10. See also WILLIAM H. PAGE, 2 SUPPLEMENT TO THE LAW OF CONTRACTS 2390 (2nd ed., 1929) (stating that the "obligation of a contract" has been defined as "the duty of performance which the law demands.").

16 Hunting, *supra* note 7, at vii (referring to "the privilege of being a corporation, the privileges of engaging in certain public service businesses such as that of common carriage, the privilege of exercising the state's power of eminent domain, the privilege of using the public streets and highways for tracks, pipes, wires, etc.; and also to those privileges which may be distinguished from 'franchises' by the designation of 'immunities,' such as the immunity or exemption from taxation by the state, or from rate regulation.").

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thought to be prior and superior to the governmental entities themselves, and not a mere concession to the citizens. In particular, the Contract Clause restriction was addressed to the governments (state and federal), but not explicitly to the United States Congress.

1.2. Origin of Chile's *Intangibilidad* of Contracts Doctrine

1.2.1. Civil Law-Based Criteria Historically Utilized by Chilean Courts to Protect Contracts

Chilean legislation follows the traditional French civil law model regarding the protection of property rights. The Chilean Civil Code adopts the civil law distinction between “consolidated rights” and “mere expectations of future rights.” While the first category creates property rights, the second does not. Consequently, the legislature may not infringe upon “consolidated rights,” but it may regulate “mere expectations” without creating substantive limitations on property rights. In a sense, legislation can only affect future conduct and relations; and any law regulating past situations is deemed retroactive and deprives citizens of their legitimate property rights.¹⁷ However, the practical difficulties involved when drawing a distinction between “consolidated rights” and “mere expectations” has led Chilean courts to seek other criteria to identify infringements on property rights by retroactive legislation.

Among the main theories, all of them drawn from European jurisprudence, to which Chilean courts have resorted to avoid legislative encroachment on contracts, we find the following:

1.2.1.1. The “Essential Content” Theory

This is one of the most classic categories utilized by contemporary European constitutional law. The “essential content” of a right includes those elements that configure the very identity of the right. Chilean authors have defined the

“essential content” of the right to property as composed by two elements. The first is called “*atributos del dominio*” and includes the main characteristics of the rights to property itself: (i) generality; (ii) perpetuity; and (iii) exclusivity. The second element is the “*facultades del dominio*,” which refers to the powers of the owner to use and freely dispose of his assets. Accordingly, any legislative violation of any of these essential elements triggers a duty to compensate the owner.

The drawback of this theory is that it requires an abstract analysis of the essential content of the right to property without any concrete reference to the facts of a given case. In particular, after –in abstract– defining what constitutes the essential content of the property right, the judge determines whether the legislation at stake merely “regulates” or “deprives” the owner of that essential content. A mere “regulation” does not create a duty to compensate the owner. Instead, a deprivation of what constitutes the “essential content” does create that right. For example, in 1996 a presidential decree mandated that all landlords owning land adjacent to beaches to provide free access to the general public to the beach. The Chilean Constitutional Tribunal declared that decree unconstitutional because it deprived landlords of their capacity to freely dispose of their property.¹⁸ This decision did not consider the concrete aspects of the case but was based on an abstract analysis of the essential elements of the right to property.

This “abstract” analysis has been heavily contested by Chilean constitutional scholars,¹⁹ on the bases that it does not include a reference to the type of property involved, no consideration is given to the foreseeability of the regulatory change, and no analysis of the economic impact of the challenged measure is offered. It is further argued that the “essential content” analysis focuses on a theoretical threshold between the “core” and the “penumbra” of the right to property.

¹⁸ Chilean Constitutional Tribunal, Case No. 245/246 (1996) (Chile).

¹⁹ ARTURO FERMANDOIS, *DERECHO CONSTITUCIONAL ECONOMICO* 317 (2010).

¹⁷ LON FULLER, *THE MORALITY OF LAW* 80-81 (1969).

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However, in spite of this criticism, the framers of the Chilean constitution considered this theory during the debates leading to the drafting of the constitutional provisions over property rights. Undoubtedly, this criterion has also influenced the Chilean Tribunal in many opportunities.

Ultimately, the “essential content” standard has been progressively abandoned by other more flexible criteria.²⁰

1.2.1.2. The “Legitimate Expectations” Principle

This principle has also been taken from European jurisprudence. It applies when an unpredictable or sudden regulatory change affects property rights. This theory imposes on legislatures the duty to honor reasonable expectations created by the law. This principle is based on the idea of the rule of law itself: one of the main functions of the law is to guide the behavior of the governed, allowing them to regulate their own affairs in a manner conforming to the law. Therefore, any modifications of the current legislation must carefully protect the interests created for private citizens in their relations under the protection of a law in force at the time the contract was entered into.²¹

This governmental duty to act fairly demands from the legislator the elaboration of transitional rules that must be included in a piece of legislation that contains regulatory changes.²²

²⁰ A good example is the decision issued by the Chilean Constitutional Tribunal in the case, HQI Transelec S.A. v. Empresa Eléctrica Panguipulli S.A., where the Constitutional Tribunal decided in favor of the constitutionality of a law that modified the way in which an electric company calculated the price of its services. Even though the price is an essential element of the contract, the economic consequences of the change were not sufficient to consider the legislative measure as a violation of property rights. Tribunal Constitucional [T.C.] [Constitutional Court], 6 marzo 2007, “HQI Transelec S.A. v. Empresa Eléctrica Panguipulli S.A.,” Rol de la causa: 505-06 (Chile) available at available at: http://www.tribunalconstitucional.cl/wp/descargar_expediente.php?id=22955.

²¹ See generally *The Rule of Law and Its Virtue*, in JOSEPH RAZ, *THE AUTHORITY OF LAW: ESSAYS ON LAW AND MORALITY* 212-213 (1979).

²² See Paul Yowell, *Legislation, Common Law and the Virtue of Clarity*, in *MODERN CHALLENGES TO THE RULE OF LAW* 101 (Richard Ekins, ed., 2011) (analyzing the importance of transitional rules, and confronting the differences between congressional and

The absence of these rules would create a context in which the government would have the obligation to compensate those whose property is being affected by the unexpected legal change. However, this is not the only case in which the government would compensate a victim based on the principle of “legitimate expectations.” European courts have established the following criteria for the application of this theory: (i) When there is a law that publicly encourages citizens and companies to develop a specific kind of business; in this situation, the law has to place the citizens and/or their companies in a favorable situation; (ii) The favorable situation must have its origins in a lawful act of government; (iii) The law must create a regime of confidence; that is, the beneficiaries should not reasonably expect a sudden legal change; and (iv) The existence of an unforeseen legal change that breaks this context of confidence, producing economic injury to investors.

Under the described conditions, European courts have ordered governments to pay due compensation.²³

This criterion is eminently concrete. It requires an adequate study of the terms of the law, the circumstances under which the confidence arises, the economic impact of the legal change, and the foreseeability of it. This is the reason why it is difficult to explain this doctrine on a purely abstract level. Chilean courts have been very conservative regarding the application of this criterion to protect contractual and property rights from unforeseen legislative changes. However, it is possible to find some cases where the courts applied the principle, but without mentioning it.²⁴

judicial legislation. In his view, whereas legislatures have the chance to establish transitional rules, protecting private interests, courts cannot do so).

²³ The European Court of Justice, for example, has used the “legitimate expectation” principle to condemn States in cases such as Case T-20/91, *Holtbecker v. Commission*, 1992 E.C.R. II 2600, and Joined Cases C-104/89 and C-37/90, *Mulder and Others v. Council and Commission*, 2000 E.C.R. I 288. See: www.eur-lex.eu.

²⁴ One of those cases is the *Galletue* case (Chilean Supreme Court, August 7, 1984), which reviewed the constitutionality of a governmental declaration of the *araucaria araucana* (a native Chilean tree) as endangered vegetal species under the protection of the law. The declaration had the effect of preventing any person or company from economically exploiting that natural resource, thus affecting a group

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1.2.1.3. The Proportionality Principle

The proportionality principle is one of the most important legal standards used today by domestic and international courts. It has also been applied to protect property rights from regulatory changes. The proportionality principle obliges the legislature to restrict rights, such as the right to contract and the right to property, in an appropriate way. The intensity of the restriction has to adequately respond to the social importance of the limited rights. There must be a relationship of proportionality between them.

The proportionality test is composed by two essential parts. First, any restriction must be directed to a “sufficient,” “pressing,” or “important” social objective. Second, the government must demonstrate that the means used to restrict the right are reasonable and justifiable. A restriction would be reasonable and justifiable if: (a) the measure is carefully designed to achieve the legislative purpose; (b) it impairs as little as possible the exercise of the right; and (c) the legislative measure is proportional itself, considering the importance of the right at stake. This implies an exercise of judicial balancing between the protected interest and the restricted right.

Since 2006, the Chilean Constitutional Tribunal has applied the proportionality test in different contexts. For example, it has been used to decide (a) whether a civil penalty is constitutional; (b) whether an administrative

of persons in the South of Chile who had previously invested large amounts in related businesses. The Chilean Supreme Court decided that the affected people had to be compensated for the damages produced by this unexpected normative change. See Corte Suprema de Justicia [C.J.S.] [Supreme Court], 7 agosto 1984, “Comunidad Galletúe con Fisco” [Community of Galletúe v. The Treasury], REVISTA DE DERECHO Y JURISPRUDENCIA, UNIVERSIDAD CATÓLICA DE VALPARAÍSO, TOMO XI, 1987 at 67 (Chile). Likewise, Chilean appellate courts have applied the principle of “legitimate expectations” concerning the issue of public licenses to develop economic activities (see, e.g., Corte Suprema de Justicia [C.J.S.] [Supreme Court], 27 octubre 2005, “Sibilia Contreras, Elizabeth y otro con Municipalidad de Antofagasta y otro (recurso de protección)” [Elizabeth Sibilia Contreras and others versus the Municipality of Antofagasta and others (protection of resource)], REVISTA DE DERECHO Y JURISPRUDENCIA, Núm. 2-2005, diciembre 2005.).

measure deprives a citizen of a welfare benefit; and (c) whether the modification of a contract produces unconstitutional effects concerning property rights.²⁵

The use of the proportionality principle has become a sort of “legal revolution” in a country with a very legalistic culture such as Chile. In spite of the arguments against this new criterion, the application of the proportionality test to measure the constitutionality of legislative and administrative decisions has enriched the debate about rights limitations.

1.2.2. The Emergence of the Constitutional Intangibilidad de los Contratos Doctrine

It is in this context, already analyzed, where the doctrine of *intangibilidad de los contratos*, also called the “doctrine of the sacrality of contracts,” or “doctrine of the invariability of what is legitimately agreed upon,”²⁶ made its appearance in Chilean constitutional law. The doctrine of the *intangibilidad* of contracts was not expressly mentioned in the Chilean Constitution of 1925 or in prior constitutions,²⁷ but resulted from a judicial interpretation of that Constitution. Specifically, the Chilean Supreme Court considered that the doctrine of the *intangibilidad* of contracts proceeded from the constitutional guarantee of the right to property.²⁸ The Court also clarified that government interference with contractual rights

²⁵ *Transec*, Rol de la causa: 506-06 (In *Transec*, the Chilean Constitutional Tribunal directly pondered the economic consequences of an economic regulation in order to decide about its constitutionality, thus strongly affirming the defense of property rights in Chilean law.

²⁶ JOEL GONZÁLEZ, EL DERECHO DE PROPIEDAD Y LA INTANGIBILIDAD DE LOS CONTRATOS EN LA JURISPRUDENCIA DE LOS REQUERIMIENTOS DE INAPLICABILIDAD 352 [THE RIGHT OF PROPERTY AND THE INTANGIBILIDAD OF CONTRACTS IN THE JURISPRUDENCE OF UNCONSTITUTIONALITY WRITS] (Rev. Ch. de Der., Vol. 34 No. 2, 2007) (referring to the *Transec*, Rol de la causa: 506-06) (highlighting that this decision applied, for the first time in Chilean constitutional history, the novel doctrine of proportionality, that is, a rational standard for reviewing government interference with private contracts).

²⁷ *Transec*, Rol de la causa: 506-06 at § 20.

²⁸ JORGE BARAHONA, IRRETROACTIVIDAD DE LA LEY E INTANGIBILIDAD CONTRACTUAL A PROPÓSITO DEL FALLO DEL TRIBUNAL CONSTITUCIONAL SOBRE LA DEUDA SUBORDINADA DEL SISTEMA BANCARIO 47 [NON-RETROACTIVITY OF THE LAW AND CONTRACTUAL INTANGIBILIDAD CONCERNING THE DECISION OF THE CONSTITUTIONAL TRIBUNAL ON THE SUBORDINATED DEBT OF THE BANKING SYSTEM] (Cuadernos de Extensión Jurídica, U. de Los Andes, No. 6, 2002).

The authors focus on the most significant right to contract decisions of the Supreme Courts of Chile and the USA.

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and obligations constituted an impermissible attack on the “free and spontaneous will of the parties.”²⁹ This precedent was consistently reiterated by the Chilean Supreme Court and later by the Chilean Constitutional Tribunal³⁰ when the latter was created in 1970.

Like the Chilean Constitution of 1925, the Constitution of 1980 does not contain specific language referring to the *intangibilidad* of contractual rights. As had happened under the Constitution of 1925, the protection of contractual rights has resulted from a holistic interpretation of the constitutional provisions related to the right to property, the Chilean Civil Code, and the Chilean Law on the Retroactive Effects of Laws (LREL).

Unlike the United States Constitution, the current Chilean Constitution of 1980 contains what is seen as a broad guarantee of the right to property expressed in explicit terms. In fact, the Chilean Constitution provides³¹ in article 19 §24 that:

The Constitution guarantees to all persons:

²⁹ Corte Suprema de Justicia [C.J.S.] [Supreme Court], 10 enero 1925, “Galtier con Fisco” [Galtier v. The Treasury], 23 REVISTA DE DERECHO Y JURISPRUDENCIA 520 (Chile).

³⁰ JORGE LÓPEZ, LOS CONTRATOS. PARTE GENERAL 249 [CONTRACTS. GENERAL PART] (AbeledoPerrot Legal Publishing, 2010) (stating that “Chilean case law has traditionally established the *intangibilidad* of existing contracts, denying judges the possibility to review or amend them.”). See also JORGE BARAHONA, *supra* note 26, at 47. . (citing, for example, the decision of the Chilean Constitutional Tribunal on subordinated debt: Tribunal Constitucional [T.C.] [Constitutional Tribunal], 18 febrero 1995, “Requerimiento Formulado por Diversos Diputados para que el Tribunal Resuelva sobre la Cuestión de Constitucionalidad Suscitada Durante la Tramitación del Proyecto de Ley que Deroga el Inciso Cuarto del Artículo 10 de la Ley No. 18.401, Sobre Capitalización de Dividendos en los Bancos con Obligación Subordinada, de Acuerdo al Artículo 82, no. 2, de la Constitución Política de la República” [“Unconstitutionality Writ Submitted by Several Deputies for the Constitutional Tribunal to Resolve on the Question of Constitutionality Arising During the Review of the Bill Repealing Paragraph Four of Article 10 of Law 18,401, on the Capitalization of Dividends in Banks with Subordinated Debt, According to Article 82, No.2, of the Political Constitution of the Republic”], Rol de la causa: 207 (Chile) available at <http://jurisprudencia.vlex.cl/vid/-58942848> [“Subordinated Debt Case”]).

³¹ English translation available at: <http://confinder.richmond.edu/admin/docs/Chile.pdf>

The right of ownership in its diverse aspects over all classes of corporeal and incorporeal property.

Only the law may establish the manner to acquire property and to use, enjoy and dispose of it, and the limitations and obligations derived from its social function. Said function includes all the requirements of the Nation’s general interests, the national security, public use and health, and the conservation of the environmental patrimony.

In no case may anyone be deprived of his property, of the assets affected or any of the essential faculties or powers of ownership, except by virtue of a general or a special law which authorizes expropriation for the public benefit or the national interest, duly qualified by the legislator. The expropriated party may challenge the legality of the expropriation decree before the ordinary courts of justice and shall, at all times, have the right to indemnification for economic damage actually caused, to be fixed by mutual agreement or by a judicial decision issued by said courts in accordance with the law.

The Constitution of 1980 also contains an anti-diluting provision in article 19 §26, which has been held to be closely connected with the constitutional property safeguard, which guarantees to all persons:

“The assurance that the legal precepts which, by mandate of the Constitution, regulate or complement the guarantees established therein or limit them in the cases authorized by the Constitution, shall not affect the rights in their essence nor impose conditions, taxes or requirements which may prevent their free exercise.”

As it may be seen, the constitutional protection of the right to property was expressed in the

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Constitution of 1980 in the broadest terms possible in order to cover, as the Constitutional Tribunal has stated, “the rights to use, enjoy, and dispose of property, as well as all its attributes, in the sense that any violation thereof, is a violation of the right of property as a whole.”³² The Constituent Commission that studied the draft Constitution of 1980 understood that the essence of the right to property was affected [“impaired,” in United States constitutional jargon] when “it is decided that someone other than the owner uses, enjoys, or disposes of the property, because in this manner an essential attribute of the right is affected.”³³

Consistent with this, the highest courts in Chile have consistently upheld that incorporeal property rights are protected by the Constitution of 1980. For example, in 2006 the Chilean Supreme Court held that the “debtor” (such as a purchaser or payor) has a “species of property” over the amount of the price established in a contract, and that this incorporeal right consists “in not paying more than what was agreed.”³⁴ The Constitutional Tribunal also recognized in that case that a legislative amendment of the price only “alters, regulates, and limits the mode in which the petitioner exercises its right to property,” but does not impair the essence of the right in itself.³⁵ The Court then centered its analysis on the “magnitude of the disturbance”³⁶

in order to determine whether a deprivation of property took place, but without altering the constitutional threshold of the “essence” of the right.

In sum, the *intangibilidad* of contracts doctrine is decisively recognized as the constitutional formulation of the protection of contracts under the Constitution of 1980 in Chile.

2. Conflicting Values Shaping the Constitutionality Test for Contractual Protection

2.1. Competing Views Regarding the United States “Impairment of Contractual Obligations” Analysis

The United States Supreme Court has wavered in its interpretation of the Contract Clause. Federal case law has explicitly recognized the “conflicting values” conundrum between individual rights and states’ powers in the impairment of contracts analysis.³⁷ For instance, in 1998, the United States Court of Appeals for the Sixth Circuit made an explicit reference to the conflicting values when it stated that, on the one hand, “the regulatory power of the States is not eviscerated by a *per se* ban on legislation impairing private contracts;”³⁸ and on the other, that the “Supreme Court’s Contracts Clause jurisprudence also recognizes the ‘high value’ the Framers placed ‘on the protection of private contracts.’”³⁹

All said, the United States Supreme Court

³⁷ Toledo Area AFL-CIO Council v. Pizza, 154 F.3d 307, 323 (6th Cir. 1998) (stating that “The conflicting values of protecting the right of individuals to order their affairs by contract and allowing the states to exercise “essential attributes of sovereign power” which are necessarily reserved by the states to safeguard their citizens’ are both recognized in the analytic framework used to assess Contracts Clause claims,” citing Linton v. Commissioner of Health and Env’t, 65 F.3d 508, 517 (6th Cir. 1995)).

³⁸ Toledo Area AFL-CIO Council, 154 F.3d at 322 (“Contracts Clause jurisprudence evinces a concern for ensuring that the regulatory power of the States is not eviscerated by a *per se* ban on legislation impairing private contracts[.]” and at 323 (“Citizens cannot be permitted to place *any* matters they wish beyond the reach of the state’s police power merely by entering into a contract. But the Supreme Court’s Contracts Clause jurisprudence also recognizes the ‘high value’ the Framers placed ‘on the protection of private contracts.’” [emphasis in the original]).

³⁹ *Id.*

³² Tribunal Constitucional [T.C.] [Constitutional Tribunal], 21 agosto 2001, “Requerimiento Formulado por Diversos Senadores para que el Tribunal Resuelva la Constitucionalidad del Proyecto de Ley, que Modifica el Decreto Ley No. 3.500, de 1980, que Establece Normas Relativas al Otorgamiento de Pensiones a Través de la Modalidad de Rentas Vitalicias, de Acuerdo al Artículo 82, No. 2, de la Constitución Política de la República” [Unconstitutionality Writ Submitted by Several Senators for the Constitutional Tribunal to Decide on the Constitutionality of a Bill Amending Decree-Law 3,500 of 1980, that Establishes Provisions Related to the Granting of Pensions Through the Modality of Life Annuities, in Accordance with Article 82, No.2, of the Political Constitution of Chile], Rol de la causa: 334 (Chile) available at REVISTA DE DERECHO Y JURISPRUDENCIA, Núm. 3-2001, Julio 2001, 137 [“Rentas Vitalicias Case”] at at § 12. (citing Revista de Derecho y Jurisprudencia, Tomo LXXXVI, Sección 5a, Segunda parte, at 222).

³³ Corte Suprema de Justicia [C.S.J.] [Supreme Court], 18 junio 2004, “Inmobiliaria Maullín Limitada,” Rol de la causa: 4.309 (Chile) 17 REVISTA DE DERECHO 215 at § 7 (discussing the unconstitutionality of Law 17.288 (articles 11 and 12)).

³⁴ *Transelec*, Rol de la causa: 505-06 at § 16.

³⁵ *Id.* at § 25.

³⁶ *Id.* at § 26.

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cannot overlook the text of the constitutional provision (“[n]o State shall ... pass any ... Law impairing the Obligation of Contracts”⁴⁰), or the original intent of the Founders to provide a strong guarantee for citizens vis-à-vis the government. Federal decisions have interpreted the Contract Clause accordingly; for example, in 2002 the United States Court of Appeals for the Eight Circuit held that:

The severity of an impairment of contractual obligations can be measured by the factors that reflect the high value the Framers placed on the protection of private contracts. Contracts enable individuals to order their personal and business affairs according to their particular needs and interests. Once arranged, those rights and obligations are binding under the law, and the parties are entitled to rely on them.⁴¹

However, over the early twentieth century (the “Progressive Era”) and redoubling its efforts since the New Deal, the United States Supreme Court has increasingly construed the impairment of contracts prohibition as not absolute.⁴² In fact, the Court has rejected an absolute reading precluding states from ever impairing any contracts,⁴³ based on the assumption that private parties could “contract” in such a way as to circumvent state regulatory law.⁴⁴ Accordingly, the Court

40 U.S. CONST. art I, §10, cl. 1.

41 Equipment Manufacturers Institute v. Janklow, 300 F.3d 842, 854 (8th Cir. 2002) [citing Allied Structural Steel v. Spannaus, 438 U.S. 234, 245 (1978)].

42 Lipscomb v. Columbus Municipal Separate School District, 269 F.3d 494, 503-504 (5th Cir. 2001) (stating that “The Supreme Court has emphasized, however, that the absolute language of the Contract Clause does not create an absolute prohibition; a State must be given some accommodation in passing laws ‘to safeguard the vital interests of its people.’”).

43 Baltimore Teachers Union v. Mayor of Baltimore, 6 F.3d 1012, 1014 (4th Cir. 1993) (“Though the Contract Clause is phrased in absolute terms, the Supreme Court does not interpret the Clause absolutely to prohibit the impairment of either government or private contracts.”).

44 United States Trust Co. v. New Jersey, 431 U.S. 1, 22 (1977) (“The States must possess broad power to adopt general regulatory measures without being concerned that private contracts will be impaired, or even destroyed, as a result. Otherwise, one would be able to obtain immunity from state regulation by making private contractual arrangements.”).

has aimed at preserving the states’ power to regulate private contracts, usually based on the protection of the wellbeing of the citizens,⁴⁵ and to prevent abuses such as racial discrimination, for example.⁴⁶ A further analysis of this point will be made later in this article.

2.2. Contrasting Views on Constitutional Contract Protection in Chile

The constitutional history of Chile equally shows that contrasting analyses affected the formation of the *intangibilidad* of contracts doctrine. One view (the “contract-stability approach”) stems from the reality that contracts possess an undeniable economic role and advance the need to provide for contract stability (predictability; non-volatility) in order to foster investment. The opposite view maintained instead that, in order to promote the development of the Chilean people, the legislature had to be vested with the necessary powers to introduce amendments in the legal *status quo*.⁴⁷ But by far, Chilean legal commentators have overwhelmingly recognized the contract-stability approach as the cornerstone of contractual law in Chile.⁴⁸ However, during the difficult decades of the sixties and seventies, constitutional changes reflected the tensions afflicting Chilean society. In fact, the Constitutional Amendment approved by Law 17,450 of July 16, 1971 came to alter the constitutional status of the so-

45 Energy Reserves Group v. Kansas Power & Light, 459 U.S. 400, 410 (1983), (“Although the language of the Contract Clause is facially absolute, its prohibition must be accommodated to the inherent police power of the State ‘to safeguard the vital interests of its people.’”). See also United Automobile v. Luis Fortuño, 633 F.3d 37, 41 (1st Cir. 2011) (“Rather, ‘A court’s task is “to reconcile the strictures of the Contract Clause with the essential attributes of sovereign power necessarily reserved by the States to safeguard the welfare of their citizens.’”).

46 United Healthcare Insurance Co. v. Angele Davis, 602 F.3d 618, 631 (5th Cir. 2010) (“Justifications for contractual impairments that the Supreme Court has found to be acceptable have been exercises of the state’s sovereign authority to protect its citizens and prevent abuses of its contracts.”).

47 JORGE BARAHONA, *supra* note 26, at 48.

48 JORGE OVIEDO, DERECHOS DE LOS CONTRATOS 158 [LAW OF CONTRACTS] (Hernan Corral, et al., eds.), Universidad de Los Andes Facultad de Derecho. Cuadernos de Extensión Jurídica 6, April 24, 2002. (calling the contract “the cornerstone of the free economy system [which] realizes the fundamental human values of liberty, autonomy, solidarity, and loyalty [and also as the] main instrument for the channeling of wealth, as well as a facilitator of community life.”).

Comparative Constitutional, *continued*

called “contract-laws,” that is, contracts signed between a government agency and a private party. Such reform added a few provisions to article 10 No. 10 of the Constitution of 1925, stating that:

In cases where the State or its agencies have executed or execute, with the proper authorization or approval of the law, contracts or agreements of any kind in which they commit to maintain in favor of private parties certain legal regimes of exception or special administrative treatment, these may be modified or terminated by the law when required by the national interest.

In qualified cases, when as a consequence of the application of the preceding paragraph a direct, real, and effective injury occurs, the law may provide compensation to those affected.

The Constitutional Amendment of 1971 came to recognize the legal character of contract-laws **and** to eliminate the constitutional guarantee of the right to property that had previously safeguarded them under the Constitution of 1925.⁴⁹ The Amendment also added two grounds for the impairment of contract-laws. First, to meet the contingencies of “qualified cases;” and second, to meet the contingencies of the Chilean “national interest.” Accordingly, the legislature received discretionary powers it previously lacked, thus being able to determine the ultimate validity and consequences of contract-laws, over which only cursory judicial review remained. Constitutional Act Number 3 of 1976 superseded the 1971 Amendment.

Years later, in a different political and legal ethos, it was the Constitutional Tribunal which in 2007 clearly explained the ideological reasoning justifying the constitutional protection of contractual rights. The Tribunal explicitly stated that,

From an objective point of view, the foundation of a contract is its economic profit. The pursuit of profit is the reason for people to enter into contracts. If a government regulation concerning a price deprived a party of its aim to profit, then that party would be able to sustain that it has been deprived of the essence of its property, because the core of one of the essential attributes of his property has disappeared, which is its legitimate expectation of economic benefit or profit. But the private party may not prevent a public need from amending the amount of the profit that that party was perceiving pursuant to the contract, when the legislator justifies such restriction in a requirement imposed by the public interest which is constitutionally accepted.⁵⁰

3. Development of the United States “Impairment of Obligations” Analysis

3.1. Chief Justice Marshall’s Influence on the “Impairment of Obligations” Analysis

Chief Justice John Marshall’s impact on the United States Supreme Court and American jurisprudence was singular and monumental. In the matter of contracts, Marshall’s formative influence grew from the landmark decisions addressing the impairment of contracts doctrine in *Fletcher v. Peck*⁵¹ in 1810, to *Trustees of Dartmouth College v. Woodward*⁵² in 1819. These cases are appropriate sources for learning⁵³ the contours of the impairment of contracts doctrine. It is important to highlight that until 1810 no authoritative judicial development or explanation of the Contract Clause of the United States Constitution existed. Chief Justice Marshall was the seminal figure who defined the most important issues

⁵⁰ *Transelec*, Rol de la causa: 505-06 at § 26.

⁵¹ *Fletcher v. Peck*, 10 U.S. (6 Cranch) 87 (1810).

⁵² *Trustees of Dartmouth College v. Woodward*, 17 U.S. (4 Wheaton) 518 (1819).

⁵³ See generally HUNTING, *supra* note 7, at ix.

⁴⁹ JUAN FIGUEROA, LAS GARANTÍAS CONSTITUCIONALES DEL CONTRIBUYENTE EN LA CONSTITUCIÓN POLÍTICA DE 1980 [THE CONSTITUTIONAL GUARANTEES OF THE TAXPAYER IN THE POLITICAL CONSTITUTION OF 1980] 250 (Ed. Juf. de Chile, 1985).

Comparative Constitutional, *continued*

involved in an “impairment” situation, and this jurisprudence is best reflected in the aforementioned cases.

It is difficult to state what the English law on the sovereign power to interfere with charters was prior to *Fletcher v. Peck* (1810).⁵⁴ The only early reference is found in the case of *The King v. Amery*,⁵⁵ which stated the doctrine that “the King cannot repeal a charter once granted[.]”⁵⁶ However, this case “[did] not disclose any particular theory of contract.”⁵⁷ In the United States, no specific provision of the Constitution gives the Supreme Court the explicit power⁵⁸ to invalidate a statute for conflicting with the Constitution. In effect, in *Marbury v. Madison*,⁵⁹ Chief Justice John Marshall noted, as an *obiter dictum*, that the United States Constitution gives to the President the discretion to make certain decisions, and the President’s exercise of that discretion in those matters is not reviewable by the judiciary.

In *Fletcher*, the Supreme Court exercised what it believed were its implicit powers and annulled state legislation that impaired valid contracts, thus establishing the so-called “doctrine of the sanctity of contracts.”⁶⁰ Delivering the majority opinion, Chief Justice Marshall famously said that, “When, then, a law is in its nature a contract, when absolute rights are vested under that contract, a repeal of the laws cannot divest those rights; and the act of annulling them, if legitimate, is rendered so by a power applicable to the case of every individual in the community.”⁶¹ In fact, the *Fletcher* decision clarified that states are bound to one another and to the United States by an agreement or compact, and this agreement or compact is the Constitution, which is the

superior law⁶² governing both the United States and the individual states. In Marshall’s view, a legislative grant of land amounted to a contract,⁶³ and a grant “amounts to an extinguishment of the right of the grantor, and implies a contract not to re-assert that right.”⁶⁴ Marshall highlighted that the Founders conceived of the Contract Clause as a bulwark against the “violent acts which might grow out of the feelings of the moment[.]”⁶⁵ Marshall added that the restrictions imposed over state legislatures were “obviously founded” on the sentiment that “the people of the United States, in adopting that instrument [the United States Constitution] have manifested a determination to shield themselves and their property from the effects of those sudden and strong passions to which men are exposed.”⁶⁶ In consequence, a statute revoking such grant impaired the obligation of a contract, violated the sanctity thereof, and was unconstitutional.⁶⁷ In sum, *Fletcher*’s interpretation of the Contract Clause set the precedent, restraining the actions of state legislatures “to impair the obligation of contracts in an unconstitutional manner,”⁶⁸ and operated to substantially limit states’ powers.⁶⁹ Throughout the centuries,⁷⁰ courts have confirmed the importance given by *Fletcher* to contracts.

Two years after *Fletcher*, Marshall revisited the impairment of contracts doctrine in *New Jersey v. Wilson*⁷¹ (1812), and “declared that a contract which had been made between the colony of New Jersey and the Delaware Indians exempting lands from taxation was

54 *Id.* at 35.

55 *The King v. Amery*, 2 Durnford & East, 569.

56 HUNTING, *supra* note 7, at 36.

57 *Id.* at 36.

58 Joseph M. Lynch, *Fletcher v. Peck: The Nature of the Contract Clause*, 13 SETON HALL L. REV. 1, 9 (1982).

59 *Marbury v. Madison*, 5 U.S. (1 Cranch) 137 (1803).

60 Hagan, *supra* note 10, at 40.

61 *Fletcher v. Peck*, 10 U.S. (6 Cranch) 87, 135 (1810).

62 HUNTING, *supra* note 7, at 40.

63 Hagan, *supra* note 10, at 2.

64 *Id.* at 27.

65 Lynch, *supra* note 58, at 15.

66 *Id.*

67 HALL, *supra* note 3, at 513.

68 *See generally* Hagan, *supra* note 10, at 28-29.

69 *See generally* Lynch, *supra* note 58, at 18.

70 *Baltimore Teachers Union v. Mayor of Baltimore*, 6 F.3d 1012, 1016 (4th Cir. 1993)

(“Given the value ascribed to contracts in our society, and the Constitution’s explicit proscription on the state’s impairment of contracts, we would not hold, absent the clearest evidence, that the City intended to confer upon the Board of Estimates even the power unilaterally to modify the City’s contracts.”).

71 *New Jersey v. Wilson*, 11 U.S. (7 Cranch) 164 (1812).

Comparative Constitutional, *continued*

enforceable.”⁷² This decision, however, did not address the issue of “whether corporate charters as well as public grants were protected”⁷³ by the Constitution, that is, whether charters granted by the federal or state government could be considered as common law contracts.⁷⁴ The *Dartmouth College* decision of 1819 would put this topic to rest a few years later.

In *Terret v. Taylor*⁷⁵ (1815), Justice Joseph Story, a key ally of Chief Justice Marshall on the Supreme Court, held that “state legislatures had no authority to repeal the charters of private corporations, although the same could not be said of public corporations.”⁷⁶ Justice Story envisioned a different treatment of public and private charters. This perspective would grow even stronger over the years at the Supreme Court as we will see *infra*. In the case of *Sturges v. Crowninshield*⁷⁷ (1819), the Supreme Court held that a state bankruptcy law had impaired the obligation of contracts entered into prior to the law’s enactment.⁷⁸ In fact, this decision prompted the Congress to pass a federal law regulating bankruptcy.⁷⁹

But it is the *Fletcher* decision that is said to have established the principle that a grant is a contract, which, with all its originality and strength, the *Dartmouth* decision merely applied to a corporate charter.⁸⁰ The issue that the *Dartmouth* decision addressed was the extent to which state legislatures could interfere with private contractual relationships. This debate centered around the determination of whether a charter of incorporation or a grant – as emanations of the State’s power to authorize franchises and immunities— were contracts. A related issue was whether the Contract Clause of the Constitution protected such grants. Those

who propounded the legal omnipotence of the legislature in its power to grant franchises, privileges, and grants of land obviously denied that a grant was a contract.⁸¹ In their view, an agreement not to revoke a grant would have no legal bases.⁸² Nevertheless, the Supreme Court sided with Dartmouth College and established the doctrine that all charters of private corporations are contracts within the protection of the Contract Clause of the Constitution,⁸³ and are to be considered as private property,⁸⁴ and a “vested right.”⁸⁵ Chief Justice Marshall, speaking for the Court’s majority, held that the charter incorporating Dartmouth College that had been granted by the British Crown in 1769 constituted a contract with the English State, and that the obligation passed to the State of New Hampshire upon the independence of the United States from Great Britain.⁸⁶

Next, the Supreme Court analyzed whether the contract had been “impaired” by the State of New Hampshire when it repealed Dartmouth’s charter. Marshall was building upon the tradition that in England the Crown did not have the power to “alter or repeal a grant of corporate powers,”⁸⁷ (which were then called “franchises”), and were considered as incorporeal and “a species of private property.”⁸⁸ To further his argument, Marshall alluded to the “sanctity of the corporate rights of all private corporations”⁸⁹ and reasoned that the repeal of the Dartmouth charter amounted to an unconstitutional forfeiture of property to the State.⁹⁰ In sum, *Dartmouth* established that a charter was a contract under the Contract Clause of the Constitution “by showing that it was regarded at common law as a grant of private property.”⁹¹ It is interesting to note that

⁷² HALL, *supra* note 3, at 513-514.

⁷³ *Id.* at 514.

⁷⁴ *Id.* at 516.

⁷⁵ *Terrett v. Taylor*, 13 U.S. (9 Cranch) 43 (1815).

⁷⁶ HUNTING, *supra* note 7, at 90.

⁷⁷ *Sturges v. Crowninshield*, 17 U.S. (4 Wheaton) 122 (1819).

⁷⁸ HUNTING, *supra* note 7, at 16.

⁷⁹ HALL, *supra* note 3, at 535.

⁸⁰ Hagan, *supra* note 10, at 2-3.

⁸¹ HUNTING, *supra* note 7, at 56.

⁸² *Id.* at 56.

⁸³ *Id.* at 16-17.

⁸⁴ HALL, *supra* note 3, at 505.

⁸⁵ HUNTING, *supra* note 7, at 65.

⁸⁶ *Id.* at 16-17.

⁸⁷ See generally *id.* at 69-71.

⁸⁸ See generally *id.*

⁸⁹ See generally *id.*

⁹⁰ *Id.* at 70.

⁹¹ *Id.* at 98.

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in their arguments both litigants “presented a case for limited federal activity.”⁹² *Dartmouth* is perhaps the seminal analysis on the contractual nature of charters of incorporation. Over the years, the *Dartmouth* jurisprudence has been applied to a multitude of corporations, including religious corporations, banks, and public utilities.⁹³

Therefore, we turn next to the most important progeny of *Dartmouth*, and then we will review how later developments weakened *Dartmouth* by strengthening the powers of legislatures to affect private contracts.

The progeny of *Dartmouth College* confirmed Marshall’s doctrine on the impairment of contracts. In fact, in *Green v. Biddle*⁹⁴ (1823) the Supreme Court allowed that the same protection afforded to a contract between private parties or a State and a private party⁹⁵ had to be given to a contract between two States. The later decision of *Ogden v. Saunders*⁹⁶ (1827) dealt with a novel topic for American jurisprudence. As previously mentioned, the underlying tension in the nascent impairment of contracts doctrine consisted in the different analyses of whether a contract’s validity proceeds from the free will of the parties, or is grounded in state acts recognizing the effects of a contract.⁹⁷ Marshall never hesitated in his views. He sided with the most traditional definition of a contract, which regarded it as “a compact between two or more persons[.]”⁹⁸ Marshall also stated that a grant “implies a contract not to reassert”⁹⁹ the right granted by the grantor, and consequently concluded that the annulment of a grant would be “repugnant to the Constitution[.]”¹⁰⁰

Courts and writers prior to Marshall repeatedly

answered the question of why a contract constitutes a valid and enforceable agreement before the law as having its foundation in the law of nature, that is, “Natural Law,” as explicated by scholars as dissimilar as St. Thomas Aquinas and Hugo Grotius.¹⁰¹ Natural Law “constituted the generally accepted philosophy of that day.”¹⁰² Without doubt, this was also Marshall’s legal approach to the subject.¹⁰³ *Ogden* also made clear that “the ‘obligation’ of a ‘contract’ between a State of the Union and one of its citizens ‘is founded on natural rather than municipal law.’”¹⁰⁴ Thus, the *Ogden* decision did not hesitate to hold that the law of contract arises from principles of natural or universal law and not from a concession of the government to the citizens.¹⁰⁵

When considering the aftermath of the *Dartmouth* decision and its progeny, it is generally agreed that *Dartmouth* set the standard for the development of corporate America and of an era of economic prosperity in the United States.¹⁰⁶ But the issue was far from judicially settled, as strong forces sought to counter *Dartmouth*’s influence. In fact, the biggest charge against *Dartmouth* was that its doctrine ultimately facilitated economic concentration and monopoly.¹⁰⁷

The consequent legal mechanisms designed by the States to bypass the effects of *Dartmouth* centered on the use of the reservation clause in charters of incorporation giving state governments the power to alter and amend, and this clause was generally “upheld as a public contract by the courts.”¹⁰⁸

3.2. Post-Marshall Doctrinal Transformation

⁹² HALL, *supra* note 3, at 522.

⁹³ BLACK, *supra* note 4, at 728.

⁹⁴ *Green v. Biddle*, 21 U.S. (8 Wheaton) 1 (1823).

⁹⁵ HALL, *supra* note 3, at 534.

⁹⁶ *Ogden v. Saunders*, 25 U.S. (12 Wheaton) 213 (1827).

⁹⁷ See generally HUNTING, *supra* note 7, at 22-23.

⁹⁸ *Id.* at 25.

⁹⁹ *Id.*

¹⁰⁰ *Id.*

¹⁰¹ PETER J. STANLIS, EDMUND BURKE AND THE NATURAL LAW 23-24 (2003).

¹⁰² HUNTING, *supra* note 7, at 26.

¹⁰³ *Id.*

¹⁰⁴ *Id.* at 44.

¹⁰⁵ See generally *id.* at 44-46.

¹⁰⁶ See generally HALL, *supra* note 3, at 532.

¹⁰⁷ See generally *id.* at 533.

¹⁰⁸ *Id.* at 543.

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Upon the death of John Marshall, Roger B. Taney was appointed as the new United States Supreme Court Chief Justice. Taney's judicial philosophy differed from that of his predecessor in that Taney advocated the doctrine of "dual federalism."¹⁰⁹ He eventually had the opportunity to apply his views in *Charles River Bridge v. Warren Bridge*,¹¹⁰ where he maintained that a grant was revocable at the will of the legislature. In this way, Taney recognized the primacy of State action over the rights of a private corporation.¹¹¹ Justice Story, still a member of the Court, expressed his dissent in strong terms, and demanded the Court's return to "the principles of natural justice which the earlier Marshall Court had enunciated in shaping the ends of central government."¹¹²

A critical development occurred in 1863, when the Supreme Court held in *Gelpcke v. Dubuque*¹¹³ that "the validity and obligation of the contract is determined by state law[.]"¹¹⁴ Marshall's influence noticeably ebbed in 1879, when the Supreme Court in *Stone v. Mississippi* held that "[p]ublic corporations ... are creatures of the State which organized them, and they can be revoked by the will of the legislature [and such arrangements] are mere privileges and not rights." However, the nimbus of Justices Marshall and Story's "sanctity of contracts doctrine" was finally tarnished when the Great Depression forced the Supreme Court to rapidly change course.¹¹⁵ In particular, it was during Chief Justice Charles Evans Hughes' tenure (1930-1941) that the Supreme Court repudiated the Marshall-Story legacy regarding the Contract Clause.¹¹⁶

4. The Concept of "Contracts" Used in Both the United States and Chilean Constitutions

¹⁰⁹ *Id.* at 536-537.

¹¹⁰ *Charles River Bridge v. Warren Bridge*, 36 U.S. (1 Peters) 420 (1837).

¹¹¹ HALL, *supra* note 3, at 539.

¹¹² *Id.* at 541.

¹¹³ *Gelpcke v. Dubuque*, 68 U.S. (1 Wall.) 175 (U. S. 1863).

¹¹⁴ HUNTING, *supra* note 7, at 51.

¹¹⁵ HALL, *supra* note 3, at 543.

¹¹⁶ *See generally id.* at 543-544.

4.1. The Notion of "Contracts" in the United States Constitution's Contract Clause

The definition of "contract" for constitutional purposes is a highly complex topic in the United States.¹¹⁷ At the beginning of the nineteenth century there was no general contract law¹¹⁸ in American legal theory. Furthermore, the entire expression "obligation of contracts" is said to have been "foreign to common law[.]"¹¹⁹ To some extent, the concept of "contracts" was influenced by European continental scholarship then extant in the British colonies and the early American Republic.¹²⁰

In this context, it is worth noting that when Chief Justice Marshall decided the early Contract Clause cases, presumably he did not have access to the minutes of the United States Constitutional Convention, since these "were secret and [the Convention's] Journal was not published until 1819."¹²¹ In turn, James Madison's notes were not published until 1836.¹²²

Chief Justice Marshall himself paid great attention to writings elaborating on the Roman law concept of obligation.¹²³ Furthermore, as already stated, Marshall apparently embraced the idea that the law of contracts could be deduced from the "law of nature."¹²⁴ Marshall's assumptions were built around the notion that "it is not the state that gives the validity and force to the contract, but, conceivably, a contract that gives validity and force to the state."¹²⁵ In other words, in Marshall's view, "individuals do not derive from government their right to contract, but bring that right with them into society;

¹¹⁷ *See generally* HUNTING, *supra* note 7, at 12-13.

¹¹⁸ *See generally* Nathan Isaacs, *John Marshall on Contracts. A Study in Early American Juristic Theory*, 7 Va. L. Rev. 413, 414 (1921).

¹¹⁹ *Id.* at 418.

¹²⁰ *See generally id.* at 418-419.

¹²¹ Hagan, *supra* note 10, at 35.

¹²² *Id.*

¹²³ Isaacs, *supra* note 118, at 419.

¹²⁴ *See generally id.* at 421.

¹²⁵ *Id.*

Comparative Constitutional, *continued*

that obligation is not conferred on contracts by positive law, but is intrinsic, and is conferred by the act of the parties.”¹²⁶ In *Ogden v. Saunders*, Marshall predicted, “[I]f the majority opinion prevailed [that a government grant was not a contract], States would soon be nullifying an important clause of the Constitution by merely declaring that all contracts shall be made subject to the existing laws of the State, and any modifications thereof that the State may see fit to make.”¹²⁷

Eventually, Marshall’s prophecy was fulfilled when States began to insert the “alter, amend or repeal clause” in charters, and later in state statutes and state constitutions abrogated the federal constitutional principles¹²⁸ which Marshall had enunciated in the *Dartmouth* decision, as will be reviewed *infra*.

It is important to remember that also in *Dartmouth* (1819), Justice Story posited a more Roman law-oriented analysis of contractual protection when he discussed the doctrine of vested or “acquired” rights.¹²⁹ In fact, contrary to traditional common law theory, Story found that mere gratuity constituted valuable and sufficient consideration for the creation of a valid contract between parties. In the case at hand, Story argued, the fact that the British Crown had “granted” Dartmouth College a charter, receiving nothing back in exchange, made the charter no less than a contract which, based on Traditional Natural Law, had to be respected by the government that succeeded the British Crown after the American War of Independence. Justice Story thus parted company with the singular, overly Calvinist notion that denied validity to the free intention of the contracting parties expressed in mere gratuity or beneficence,¹³⁰ contrary to Natural Law and to Roman law principles.¹³¹ In subsequent cases, Justice Story, who “was far

in advance of the legal thinkers of his day[,]”¹³² consistently sought to protect property rights from government intrusion.

As already mentioned, the *Ogden* decision dealt with a state insolvency law discharging debtors from liability stemming from their contracts. The United States Supreme Court held that for a contract between a state and a private party to be protected, the contract must be permitted by the law of the state.¹³³ This was the first departure from the *Dartmouth* doctrine on the nature of contracts, in the sense that, simply put, the Court sustained that the source of legitimacy of contracts resided in positive law and in an act of the government, i.e., the state, and not in Natural Law.¹³⁴ Justice Marshall had reaffirmed that the concept of obligation,¹³⁵ which common law writers admitted originated in Roman law,¹³⁶ “was a fundamental conception of that law[.]”¹³⁷

In light of this jurisprudence critical of state action, a technical device called “the reservation clause,” already alluded to, began to be utilized. The reservation clause consisted in the insertion of a provision in charters and statutes that recognized the power of the legislature to repeal such charter or statute, and that that action could not be impaired by subsequent legislation.¹³⁸ In this way the reservation became “a part of the contract[.]”¹³⁹ but in order to be valid, it had to be entered into prior to the time when “the charter or franchise [was] granted,”¹⁴⁰ and it could not impair the rights of third parties.¹⁴¹ An effect of the reservation clause was to deprive private parties

¹²⁶ *Id.* at 424 (citing *Ogden v. Saunders*, 25 U.S. (12 Wheaton) 213 (1827)).

¹²⁷ *Id.* at 425-6.

¹²⁸ *Id.* at 427.

¹²⁹ See generally HALL, *supra* note 3, at 526.

¹³⁰ See generally *id.* at 523-525 (analyzing Justice Story’s opinion).

¹³¹ See generally *id.* at 523-527.

¹³² *Id.* at 533.

¹³³ HUNTING, *supra* note 7, at 41.

¹³⁴ HUNTING, *supra* note 7, at 115 (“the most eminent jurists of the day ... [referring to the Constitutional Convention and the years thereafter] were firm adherents to the doctrine of natural law.”).

¹³⁵ *Id.* at 42.

¹³⁶ *Id.* at 25-26.

¹³⁷ *Id.* at 19.

¹³⁸ See generally JAMES F. DONNELLY, A TREATISE ON THE LAW OF PUBLIC CONTRACTS 132-133 (Boston, 1922).

¹³⁹ BLACK, *supra* note 4, at 730.

¹⁴⁰ PAGE, *supra* note 15, at 2399.

¹⁴¹ *Id.* at 2400.

Comparative Constitutional, *continued*

from contracting away the states' police power through private agreements.¹⁴² This would be the case, for example, if parties agreed to freeze public utility rates.¹⁴³ The counterweight to this restriction was that police powers are subject to stringent limitations in the sense that the reservation clause may not be used to alter shareholders' rights,¹⁴⁴ nor:

...as a means of forcing the corporation into enterprises not contemplated by the charter nor to take away the property of the corporation or to destroy its value, nor to impose unjust burdens upon it, nor to deprive it of rights not granted by the charter, nor, generally, to withdraw from it the protection and benefit of any constitutional guaranties [sic].¹⁴⁵

But whatever the evolution of the theory of contracts and their legitimacy for purposes of constitutional analysis in the United States, the centrality of the essence of contracts was clear at Marshall's time and afterwards. In the eighteenth century Blackstone placed contracts under "conveyances," because "a contract is one of a dozen modes of producing an effect on the title of property."¹⁴⁶ In 1810 in *Fletcher*, Justice William Johnson held in his partial dissent that "There can be no solid objection to adopting the technical definition of the word 'contract,' given by Blackstone."¹⁴⁷ Furthermore, he added that "The etymology, the classical signification, and the civil law idea of the word, will all support it."¹⁴⁸ Professor Theophilus Parsons, in turn, stated in 1853 that, "Almost the whole procedure of human life implies ... the continual fulfillment of contracts."¹⁴⁹ In this same vein, Sir Henry Maine said in 1861 that, "the progress of all civilization was 'from status to contract.'"¹⁵⁰

¹⁴² *Id.*

¹⁴³ *Id.* at 2401.

¹⁴⁴ BLACK, *supra* note 4, at 730.

¹⁴⁵ *Id.* at 730.

¹⁴⁶ Isaacs, *supra* note 118, at 415.

¹⁴⁷ *Fletcher v. Peck*, 10 U.S. (6 Cranch) 87, 144 (1810).

¹⁴⁸ *Id.*

¹⁴⁹ Isaacs, *supra* note 118, at 415.

¹⁵⁰ *Id.* at 416.

4.2. The Notion of "Contracts" for the Intangibilidad Analysis in the Chilean Constitution

In Chile, the principal and most traditional statutory authority regulating contracts is the Civil Code of 1857.¹⁵¹ Article 1545 of that Code provides that: "[A]ny contract entered legally is a law for the parties, and may not be invalidated except by mutual consent or for legal reasons." Therefore, the underlying rationale of Article 1545 is the protection of contracts between private parties, taking into consideration the broadest possible notion of contract.

Furthermore, article 12 of the Chilean Law on the Retroactive Effects of Law (LREL), mentioned *supra*, provides that all laws existing at the time of a contract's execution become part of that contract, thus further strengthening private agreements. This norm states that: "All rights *in rem* acquired under a law in conformity to it, subsist under the rule of another; but with respect to its privileges and burdens, and the extinction thereof, the provisions of the new law shall prevail."

The rationale of LREL article 12 is that when contracting parties set the terms of their agreements, they take into account not only those circumstances existing at the time when the agreements are made, but also the eventualities that may arise after its execution and during their performance.¹⁵²

Article 12 of LREL was not without criticism under the Constitution of 1833. In fact, as a scholar observed, "it is impossible to reconcile the contradictory points that [i] the law may impose a new means to terminate a right *in rem*, without being considered as a taking [and yet that, in addition] [ii] the '*privileges and burdens*' could not refer to the essential

¹⁵¹ CLAUDIA BAHAMONDES ET AL., PROYECTO PRINCIPIOS LATINOAMERICANOS DE DERECHO DE LOS CONTRATOS. INFORME CHILE 1 [LATIN AMERICAN PRINCIPLES ON CONTRACTS LAW. CHILE REPORT], available at:

http://www.fundacionfueyo.udp.cl/archivos/catedra_der_cont_informe_chile.pdf

¹⁵² JORGE BARAHONA, *supra* note 28, at 52.

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attributes or powers of ownership.”¹⁵³ In due course, an author warned, LREL article 12 “may also become a restriction on the maximum *intangibilidad* afforded to a contract.”¹⁵⁴ Nevertheless, none of these criticisms did away with the broad conception of the contract utilized by the Supreme Court of Chile and later by the Chilean Constitutional Tribunal in their constitutional analyses.

5. Contracts Covered by Constitutional Protections

5.1. Contracts Protected by the United States Constitution

The point of whether the Contract Clause referred solely to contracts between individuals (private contracts) or also to contracts between individuals and the state (public contracts) was hotly debated during the period of the drafting and ratification of the United States Constitution.¹⁵⁵ On the one hand, a participant in that debate referred to the “calamities [that] have been produced by frequent interferences of the state legislatures with private contracts.”¹⁵⁶ Another participant posited that the proposed language only applied to contracts between individuals.¹⁵⁷ Patrick Henry, a representative to the Virginia [Constitutional] Ratifying Convention of 1788, maintained that the contract clause referred to “public contracts, as well as private contracts between individuals.”¹⁵⁸

The same debate was refined by references to non-State interference with private contracts that are executed *bona fide*, and without fraud,¹⁵⁹ or misrepresentation.¹⁶⁰ Eventually, the record shows that the Convention sought to protect the contracts of private individuals

from retrospective laws.¹⁶¹ Justice Samuel Freeman Miller explained in his lectures on the Constitution that the Contract Clause of the Constitution was designed to “protect private contracts,”¹⁶² that is, those signed by private individuals and entities.

In 1927 Henry Campbell Black, author of, *inter alia*, the original Black’s Law Dictionary, identified four categories of contracts protected by the Contract Clause: “(a) Agreements or compacts of the state with another state. (b) Contracts of the state with corporations or individuals. (c) Grants of property or franchises by the state. (d) Contracts between private persons.”¹⁶³ It was accepted then that when a person receives the grant of a franchise and acts on it, such franchise becomes protected by the Contract Clause.¹⁶⁴ On the other hand, private contracts were broadly conceived to include agreements between a corporation and its shareholders, mortgages, negotiable instruments, and leases, *inter alia*. Contracts of a State with individuals were thought to include those for the construction of public works, government procurements, or business dealings of any sort. However, it is generally accepted that the Contract Clause does not apply to statutory grants of licenses¹⁶⁵ or to public offices,¹⁶⁶ or to contracts that are illegal, immoral, or contrary to public policy,¹⁶⁷ and that neither does the Contract Clause apply to judicial decisions, nor to the status created by marriage,¹⁶⁸ since marriage has been long “regarded as an institution of society[.]”¹⁶⁹ A

¹⁶¹ Hunting, *supra* note 7, at 120.

¹⁶² *Id.* at 110 (citing MILLER ON THE CONSTITUTION [LECTURES ON THE CONSTITUTION OF THE UNITED STATES], at 555).

¹⁶³ BLACK, *supra* note 4, at 714.

¹⁶⁴ *Id.* at 717.

¹⁶⁵ PAGE, *supra* note 15, at 2381 (stating that “a license to practice a profession, or to operate a motor vehicle, or to carry on a given business, or to operate a social club, is not a contract.”).

¹⁶⁶ BLACK, *supra* note 4, at 722 (mentioning the election or appointment of a public officer and his acceptance). *See also* PAGE, *supra* note 15, at 2384 (alluding to the abolishment of a public office, the transference of official duties, the addition of new duties, changes in salaries, requirements of posting a bond).

¹⁶⁷ BLACK, *supra* note 4, at 723.

¹⁶⁸ *Id.* at 714.

¹⁶⁹ *Id.* at 724.

¹⁵³ *Id.* at 53.

¹⁵⁴ *Id.*

¹⁵⁵ HUNTING, *supra* note 7, at 113.

¹⁵⁶ *Id.* at 112-113

¹⁵⁷ *Id.* at 113.

¹⁵⁸ *Id.*

¹⁵⁹ *Id.* at 114.

¹⁶⁰ BLACK, *supra* note 4, at 720.

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license, in turn, is commonly conceived of as “a permission granted to an individual to do some act or engage in some occupation which, without such permission, would be unlawful [and it is] not a contract.”¹⁷⁰

To summarize, the Contract Clause was originally thought to apply to contracts between a State and a private party, and not to contracts between private parties or between two States, or between a State and the United States. As a scholar put it, the essence of the Contract Clause of the Federal Constitution was, therefore, “to restrict the powers of the State Legislature(s).”¹⁷¹ As already seen, such an approach significantly changed over time.

5.2. Contracts Protected Under the Chilean Constitution

Private contracts and public contracts [called *contratos-ley*] are both protected under the Chilean Constitution of 1980.

5.2.1. Legal Reasoning Underlying the Constitutional Protection of Private Contracts in Chile

As already mentioned, the Chilean Constitution of 1980 does not contain an explicit guarantee of private contractual rights. Nonetheless, the Chilean Supreme Court has protected contractual rights based on two premises. First, the Court maintains that the constitutional protection of the right to property covers all types of corporeal and incorporeal property.¹⁷² And second, the Supreme Court adheres to the notion that rights arising from contracts [contractual rights], when validly executed, become a part of the patrimony of the contracting parties, and thus “remain immediately and automatically protected and covered by the right to property”¹⁷³ guaranteed

by article 19 §24 of the Chilean Constitution of 1980. The extrapolations of the Chilean Supreme Court complement the limit to the retroactive application of the laws in Article 19 §24 of the 1980 Constitution.¹⁷⁴

Under the original text of the Chilean Constitution of 1925, the Supreme Court ruled consistently that the guarantee of “inviolability of all properties”¹⁷⁵ implicitly encompassed incorporeal property, viz., contractual rights. For example, in 1968 the Supreme Court declared the unconstitutionality of a law that, without compensation, extended the terms of rural lease agreements executed before its promulgation, on the ground that the law violated the landlord’s right of ownership over the personal right that arose from the contract allowing him to request the restitution of his property within the term contractually agreed to prior to the law.¹⁷⁶

Ultimately, the highest courts of Chile have built the protection of contractual rights according to the joint interpretation of, *inter alia*, articles 12 and 22 of LREL. For example, in 1995 the Constitutional Tribunal declared unconstitutional a bill seeking to ban bank shareholders who held subordinated debts with the Chilean Central Bank from re-capitalizing (reinvesting) profits. Under the prior law and pursuant to existing stock purchase agreements, shareholders enjoyed a preferential right to re-capitalize their dividends, and in this way avoid the payment of the debts owed to the Central Bank. The Constitutional Tribunal reasoned that, pursuant to article 12 of LREL, the prior law allowing shareholders such right had become “incorporated” into the stock purchase agreements, that is, it had become an “acquired right” in accordance with LREL’s language. Furthermore, the Tribunal held that such rights were protected by the constitutional guarantee

¹⁷⁰ *Id.* at 721.

¹⁷¹ See generally HUNTING, *supra* note 7, at 51.

¹⁷² *Rentas Vitalicias*, Rol de la causa: 334 at § 7.

¹⁷³ Miguel Fernández, *Fundamentos Constitucionales del Derecho de los Contratos: Intangibilidad, Autonomía de la Voluntad y Buena Fe* 29 [Constitutional Foundations of the Law of Contracts, Intangibility, Autonomy of the Will and

Good Faith], in DERECHO DE LOS CONTRATOS. ESTUDIOS SOBRE TEMAS DE ACTUALIDAD (Hernán Corral et al. eds; Santiago, 2002).

¹⁷⁴ JORGE BARAHONA, *supra* note 28, at 50.

¹⁷⁵ ARTURO FERMANDOIS, II DERECHO CONSTITUCIONAL ECONÓMICO. REGULACIÓN, TRIBUTOS Y PROPIEDAD 264 (Ed. Universidad Católica de Chile, 2010).

¹⁷⁶ JORGE BARAHONA, *supra* note 28, at 56-7.

Comparative Constitutional, *continued*

of the right to property,¹⁷⁷ that later laws could not unilaterally amend prior agreements,¹⁷⁸ and that the lack of compensation to shareholders constituted an unconstitutional taking of property.¹⁷⁹ Thus, the repealing law was deemed unconstitutional, not due to its retroactivity, but because it deprived the shareholders of a preferential right that they had acquired by virtue of article 12 of LREL.¹⁸⁰

An author explained that the above decision of the Constitution Tribunal “announced the doctrine that the essence of the rights in the matter of contracts ... consists in that contractual rights ... are intangible assets protected by the constitutional guarantee of property.”¹⁸¹ Constitutional and civil law scholars in Chile have broadly embraced this conclusion, which, as a commentator proposed, triggered a process of “constitutionalization”¹⁸² of contracts, i.e., that: “[I]n Chilean law, the basic statute of the contract is no longer found in the principles and norms of the Civil Code, which has become a secondary regulation, but in the constitutional guarantee of property.”¹⁸³

In conclusion, a combined interpretation of articles 19 §24 of the Constitution and 12 and 22 of LREL has allowed the Chilean Supreme Court and the Chilean Constitutional Tribunal consistently to declare as constitutionally unacceptable a new law that effectively “amends, alters, or distorts the agreements existing prior

to the new law’s entry into effect.”¹⁸⁴

5.2.2. Legal Reasoning Underlying the Constitutional Protection of Public Contracts in Chile

“Contract-laws” (*contratos-ley*, mentioned *supra*), that is those executed between a private party and the state in Chile, are equivalent to public contracts in American law. The constitutional protection of “contract-laws” was hotly debated during the time prior to the Constitution of 1980. However, the Constitution of 1980 eliminated all distinctions between any types of contracts, whether public or private. The Foreign Investment Contract, which is an agreement signed between a foreign investor and the State of Chile, is the only type of contract resembling the old “contract-laws” prior to 1980 in Chile. It is generally assumed that since the Constitution of 1980 makes no distinction between any types of contracts, all of them are protected with the same types of guarantees. In other words, if the government violates a “public” contract (e.g. a Foreign Investment Contract) in Chile, it is obligated to pay damages domestically or internationally by a forum such as the International Centre for Settlement of Investment Disputes (ICSID). Nonetheless, it is important to make a brief reference to the protection of contracts-laws in Chile since it helps with understanding the current constitutional framework of contractual protection in that country.

In contract-laws the state, by virtue of its sovereign power, undertakes to respect a determined tax or other regulatory status of the private party, and to maintain this status during a certain period of time. The logical consequence is that these contracts “may only be amended by consent of both parties.”¹⁸⁵

Now, considering Chile’s highly volatile history during the past century, commentators agree that upon signing a contract-law a private party acquires an incorporeal right consisting of the

¹⁷⁷ *Subordinated Debt* Case, Rol de la causa: 207 at § 4.

¹⁷⁸ See also LUIS CLARO SOLAR, *EXPLICACIONES DE DERECHO CIVIL CHILENO Y COMPARADO 79-80* [EXPLANATIONS ON CHILEAN AND COMPARATIVE CIVIL LAW] (Ed. Jur. de Chile, Tomo I, 1978 (“the effects of the contract are governed by the law existing at the time of its execution, and are protected in case of a change of legislation.”)).

¹⁷⁹ JORGE BARAHONA, *supra* note 28, at 57-8. (Tribunal Constitucional [T.C.] [Constitutional Court], 16 julio 1982, “Sobre el Proyecto de Ley que Interpreta la Garantía Constitucional sobre Derecho de Propiedad en Relación con Reajustabilidad de Pensiones” [Bill interpreting the constitutional guarantee on the right to property as related to the adjustability of pensions], Rol de la causa: 12 (Chile), available at: www.tribunalconstitucional.cl).

¹⁸⁰ *Subordinated Debt* Case, Rol de la causa: 207 at § 2.

¹⁸¹ JORGE BARAHONA, *supra* note 28, at 58.

¹⁸² MIGUEL FERNÁNDEZ, *supra* note 173, at 23 (citing CRISTIÁN OLAVE, *RECURSO DE PROTECCIÓN* 54 (Santiago, Ed. Jurídica Conosur, 1998)).

¹⁸³ *Id.*

¹⁸⁴ *Transelec*, Rol de la causa: 505-06 at § 7.

¹⁸⁵ FIGUEROA, *supra* note 49, at 242.

Comparative Constitutional, *continued*

right to have the contract respected by the State. Accordingly, any subsequent legislative changes “are not mandatory”¹⁸⁶ for that private party’s contract-law.

However, contract-laws were strongly criticized in Chile prior to the Constitution of 1980. The main criticisms focused, first, on the incongruity of stating that an agreement could have as a source both a law and a contract.¹⁸⁷ And secondly, that the legislature lacked the authority to surrender sovereign powers belonging to the State, such as the power to pass future tax regulations.¹⁸⁸ The responses to these objections highlighted the broad practice in the Chilean legal system of the State entering into contract-laws with private parties, and that the practice constituted custom, and custom was a source of law. It was even posited that under the previous Constitution of 1925 and before the Constitutional Amendment of 1971, contract-laws were protected by the constitutional guarantee of the right to property.¹⁸⁹ Yet another counter-argument offered was that sovereign powers had the ability to self-limit themselves at any given time,¹⁹⁰ and that that was what the State did when it entered into contract-laws.

In this debate the winning position was that of the *intangibilidad* of contract-laws, which was strongly embraced by the Supreme Court under the Constitution of 1925. In a key ruling, that Court held in 1966 that contract-laws, “are legally authorized [and] possess the dual nature of public contracts and private contracts, and the State may not unilaterally terminate them, because they are bilateral agreements that produce benefits and obligations for both parties and that must be fulfilled in good faith.”¹⁹¹

This ruling was confirmed by a decision of December 27, 1968, in which the Chilean

Supreme Court confirmed that “such agreements, contracts, or conventions are created by the law.”¹⁹² Later, in a decision of July 22, 1970, the Supreme Court declared the unconstitutionality of a law unilaterally impairing the rights arising from a contract-law because that law, held the Court, “cannot be considered as a mere restriction on the use and enjoyment of the right of property.”¹⁹³ And again, in 1972, the Supreme Court held that “contract-laws are, by their nature and scope, absolutely exceptional.”¹⁹⁴

Therefore, under Chilean constitutional law, contract-laws have been historically protected, and the debate about the legitimacy over their constitutional protection is largely over.

6. Notion of “Law” for Purpose of an Impairment Analysis in both the American and Chilean Constitutions

The concept of “law” in Article I, section 10, of the United States Constitution includes State constitutions, statutes, municipal ordinances, and any amendments thereto, but not State court decisions.¹⁹⁵ In consequence, rulings or orders from non-government entities cannot impair contracts because they are not “laws” in the constitutional sense.¹⁹⁶

Chilean courts have also accepted an expansive notion of “law” for purposes of *intangibilidad* analyses. In fact, early on, in 1925, the Chilean Supreme Court recognized that courts “lacked the power to repeal or invalidate the law of contract, either based on equity, custom, or administrative regulations.”¹⁹⁷

Therefore, we see a similar broad notion of “law” for purposes of *impairment* and *intangibilidad*

¹⁸⁶ *Id.* at 243.

¹⁸⁷ *Id.*

¹⁸⁸ *Id.* at 244.

¹⁸⁹ *Id.* at 250.

¹⁹⁰ *Id.* at 245.

¹⁹¹ *Id.* at 256 (citing Rev. de Der. y Jur., tomo 63, 2a parte, sec. 1a, at 353).

¹⁹² Cited by JUAN FIGUEROA, *supra* note 49, at 257.

¹⁹³ *Id.* at 260.

¹⁹⁴ *Id.* at 258 (citing Corte Suprema de Justicia [C.S.J.] [Supreme Court], 29 junio 1972, “Decision of the Chilean Supreme Court of Justice of June 29, 1972,” (Chile) published at 69 REVISTA DE DERECHO Y JURISPRUDENCIA, 2a parte, sec. 1a, at 107).

¹⁹⁵ BLACK, *supra* note 4, at 709.

¹⁹⁶ *Id.* at 710-1.

¹⁹⁷ *Galtier con Fisco*, *supra* note 29, at ¶ 1-1.

The essentials of the contractual protection regimes in Chile and the USA are based upon noticeably congruent legal and economic principles and policies; these can ultimately be derived from traditional Natural Law.

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analyses in both the United States and Chile.

7. Twenty-first Century Constitutional Protection of Contracts in the United States and Chile

7.1. Current Constitutional Tests for the Impairment and Intangibilidad Analyses

In the case of the United States, the Supreme Court has not shown consistency in its treatment of the Contract Clause, which can be seen in the crucial aspect of determining the restrictions imposed on the States' power to enter into contracts.¹⁹⁸ Under the current doctrine, a three-factor test is utilized to determine whether a state law or regulation impairs a contract and thus violates the Contract Clause of the Constitution: (i) Whether the state law has *substantially* impaired a contractual relationship; for instance, a state regulation restricting a party to the gains it reasonably would have expected from a contract is not a substantial impairment under their three-pronged test;¹⁹⁹ (ii) After the first criterion has been met, the next stage is for the court to determine whether the state has a significant and legitimate public purpose for the regulation; for this to happen, the regulation must have been enacted to remedy a general social or economic problem and not to benefit special interests;²⁰⁰ and (iii) the court must evaluate whether the law or regulation is a reasonable and appropriate means to achieve the government's purpose; to this end—as it will be reviewed *infra*—courts treat government contracts differently from private contracts.²⁰¹ With respect to general economic and social regulation, courts defer to legislative judgment as to the necessity and reasonableness of a particular measure. Such deference is not appropriate when the state government is a party to the contract in question, because the state's self-interest is at stake.²⁰²

¹⁹⁸ See generally *Hunting*, *supra* note 7, at 51-52.

¹⁹⁹ *Energy Reserves Group v. Kansas Power & Light*, 459 U.S. 400, 411 (1983).

²⁰⁰ *Id.* at 411-2.

²⁰¹ See generally *id.* at 412-3.

²⁰² See generally *United States Trust Co. v. New Jersey*, 431 U.S. 1, 22-5 (1977).

However, this is not the only extant test on the impairment of contracts doctrine. For example, in 2010 a United States District Court mentioned a five-prong test that would include: (1) whether there is an emergency to which the legislation is responding; (2) whether past state regulation of the activity has taken place; (3) whether there is a narrow class affected by the legislation, or whether its effect is more general; (4) whether there has existed reasonable reliance on pre-existing rights by the affected parties; and (5) what has been the severity and permanency of the change produced by the law on “those relationships reasonably relied upon.”²⁰³ In 2011 another federal district court presented a four-prong test that would include different elements for an impairment determination: “In conducting this analysis, the courts have looked to (1) the terms of the contract ‘to determine whether the contract—either explicitly or implicitly—indicated that the abridged term was subject to impairment by the legislature;’ (2) whether the industry has been regulated in the past; (3) how the contract has been changed, as ‘a reasonable modification of statutes governing contract remedies is much less likely to upset expectations than a law adjusting the express terms of an agreement[;]’ and (4) ‘the character of the abridged right—whether it was by its nature the central undertaking or primary consideration of the parties.’”²⁰⁴

Nonetheless, for purposes of our analysis we will focus on the three-prong test advanced by the United States Supreme Court on impairment analyses. The following are the test's three criteria: (1) whether the state law has *substantially* impaired a contractual relationship; (2) whether the state has a significant and legitimate public purpose for the regulation; and (3) whether the law or regulation is a reasonable and appropriate means to achieve the government's purpose.

²⁰³ *Cycle Barn, Inc. v. Arctic Cat Sales Inc.*, 701 F.Supp.2d 1197, 1203 (W.D. Wash. 2010).

²⁰⁴ *Montague v. Dixie National Life Insurance Company*, 2011 WL 2294146 at *9 (D.S.C. 2011).

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Under the Chilean Constitution of 1980, it is generally accepted that, “contracts entered into by the State can only be regulated by a law,”²⁰⁵ and the law may not destroy contractual rights because they are protected by the constitutional guarantee of the right to property²⁰⁶ under the Constitution of 1980.²⁰⁷ Consequently, contract-laws may not be substantially impaired²⁰⁸ by legislation. In order to assess whether such substantial impairment has existed, in 2006 the Chilean Supreme Court announced a constitutional test for purposes of *intangibilidad* of contract-laws analysis, in the following terms: “[T]he legal regulation must be reasonable, not arbitrary, with the principle of proportionality serving as a reference for the reasonability test, which is to be *determined* by the coherent relationship between the means utilized and the legitimate purposes pursued.”²⁰⁹

The Court understood the proportionality test as composed by three criteria: a) suitability or appropriateness of the means utilized; b) necessity of the means; and c) proportionality between means and ends.²¹⁰

7.2. What Constitutes “Impairment”?

Early on, United States legal doctrine recognized that the government passes statutes restricting contracts.²¹¹ Therefore, the constitutional provision sought to circumscribe

²⁰⁵ JUAN FIGUEROA, *supra* note 49, at 252.

²⁰⁶ *Id.* at 254 (“the legal validity of the institution of contracts-laws is an unquestionable reality ... which is explicitly incorporated through the consecration of the constitutional guarantee of the right to property.”).

²⁰⁷ *Cited* in JUAN FIGUEROA, *supra* note 49, at 261.

²⁰⁸ *Id.* at 253 (stating that these contracts may not be *substancialmente afectados*—substantially impaired— by legislation).

²⁰⁹ JOEL GONZÁLEZ, *supra* note 26, at 350 (referring to Corte de Apelaciones de Santiago [Santiago Court of Appeals], 20 julio 2006, “Autopista Central S.A. con Servicio de Mecánica Mantención Track S.A.,” Rol de la causa: 541-2006 (Chile) at REVISTA DE DERECHO Y JURISPRUDENCIA, Núm. 2-2006, diciembre 2006.).

²¹⁰ *Id.* at 350 (referring to the case “Autopista Central S.A. con Servicio de Mecánica Mantención Track S.A.,” Case No. 541-2006).

²¹¹ HUNTING, *supra* note 7, at 43-4 (referring to statutes of limitations, statutes of frauds, statutes forbidding usury contracts, gambling contracts, and contracts by minors).

such restrictions in two categories: permissible and impermissible restrictions of contracts. Impermissible restrictions, or “impairments” – in the constitutional sense— included situations where a state law:

- (a) Precludes a recovery for breach of the contract.
- (b) Excuses one of the parties from performing it.
- (c) Renders the contract invalid.
- (d) Puts new terms into the contract.
- (e) Enlarges or abridges the intention of the parties.
- (f) Postpones or accelerates the time for performance of the contract.
- (g) Interposes such obstacles to its enforcement as practically to annul it.²¹²

On the other hand, it has been held that no impairment of contract exists when the law changes the remedy (the form of evidence, the method of selecting a jury or abolishing the right of appeal,²¹³ statute of limitations,²¹⁴ repeal of a usury law,²¹⁵ foreclosure, etc.) afforded to the parties to a contract and substitutes for it an entirely new remedy,²¹⁶ provided that “some *substantially equivalent remedy* is given” to the parties²¹⁷ (emphasis added). The rationale is that “the remedy is a part of the contract[,]”²¹⁸ whereas rules of evidence are not.²¹⁹

7.3. Past or Future Impairment? The Problem of Retroactivity

²¹² BLACK, *supra* note 4, at 711.

²¹³ PAGE, *supra* note 15, at 2407-2408.

²¹⁴ *Id.* at 2408 (stating that there is no impairment of contracts if the Statute of Limitations gives the party “a reasonable time after it is promulgated for bringing actions on such pre-existing contract rights.”).

²¹⁵ *Id.* at 2386.

²¹⁶ BLACK, *supra* note 4, at 737-8.

²¹⁷ PAGE, *supra* note 15, at 2406.

²¹⁸ *Id.*

²¹⁹ *Id.* at 2408.

Comparative Constitutional, *continued*

Recent United States federal case law has reiterated that the Contract Clause applies only to existing, not to future, contracts.²²⁰ Past regulatory interference with a specific industry or sector of the economy has served to vitiate a strict application of impairment analysis.²²¹ What seems to be relevant is the parties' expectation of future regulation; this is key to a determination of how substantial an impairment is.²²²

It is important to mention that the Chilean Civil Code does not contain a provision on the retroactivity of laws. The LREL filled this vacuum in 1861, that is, four years after the promulgation of the Civil Code. The LREL is based on the "traditional [retroactivity] doctrine," also called the "doctrine on acquired rights and mere expectations."²²³ The LREL established the principle of the non-retroactivity of the law²²⁴ in article 22, which provides that, "the law may only provide for the future and shall never have retroactive effect." This principle has been held to be mandatory to the Chilean State and to all of Chilean society,²²⁵ and to constitute an exclusive mandate to judges

since subsequent laws providing for retroactive effect may override the LREL or any other previous law in any given matter. However, absent a constitutionally-sanctioned non-retroactivity doctrine, it would be apparently permissible for the Chilean legislature to impair contracts by passing legislation with retroactive effects. However, as already seen, through the combination of constitutional provisions under the Constitution of 1925 and later under the Constitution of 1980, Civil Code provisions, and LREL's articles 12 and 22, Chilean courts developed a highly sophisticated doctrine aimed at protecting contractual rights under the umbrella of right to property provisions. However, that doctrine is far from being sufficiently comprehensive to protect property rights threatened under any manner of modern, complex legal, or administrative requirements.

7.4. The Three-Prong Test for Deciding an "Impairment of Contracts" in the United States

7.4.1. First Requirement: Substantial Impairment

An impairment that is not substantial, such as a state regulation that restricts a party to the gains it reasonably would have expected from a contract, does not violate the Contract Clause.²²⁶ This follows from *Allied Structural Steel Co. v. Spannaus* (1978),²²⁷ in which the plaintiff was a company whose employee pension plan was affected by a law²²⁸ that retroactively increased the monetary obligations of companies with an employee pension plan. The plaintiff argued that the new law would have the effect of either forcing the company to terminate the employee pension plan or to close its Minnesota facility. The Supreme Court ruled that the state law substantially impaired the company's contractual relations, because it had based its annual contributions to its employees' pension fund on the contractual terms, and the law retroactively modified the funding needed,

²²⁰ *Montague*, *supra* note 204, at *8 ("As interpreted, the Clause does not apply to limit the ability of state and local governments to regulate the terms of future contracts; its scope only covers government interference with already existing contracts.").

²²¹ *Campanelli v. Allstate Life Insurance Company*, 322 F.3d 1086, 1098 (9th Cir. 2003) ("In determining the extent of the impairment, a court must consider 'whether the industry the complaining party has entered has been regulated in the past.' [citing *Energy Reserves Group v. Kansas Power & Light*, 459 U.S. 400, 411 (1983).] If the industry has been heavily regulated, then the impairment is less severe because "[o]ne whose rights, such as they are, are subject to state restriction, cannot remove them from the power of the State [sic] by making a contract about them.")

²²² *Equipment Manufacturers Institute v. Janklow*, 300 F.3d 842, 857-858 (8th Cir. 2002) ("Parties' expectations of future regulation are important in determining whether contractual rights are substantially impaired because parties bargained for terms in the contract based on those expectations; if those expectations were fulfilled, the Court will not relieve parties of their obligations.").

²²³ JORGE BARAHONA, *supra* note 28, at 50.

²²⁴ *Subordinated Debt* Case, Rol de la causa: 207 at §4 ("[T]he application in this manner of the principle of no retroactivity has a considerable practical importance, since this principle alone may provide an absolute confidence in the efficacy of contracts, which is indispensable for the security of legal transactions, to which progress and social improvement are connected.").

²²⁵ *Transelec*, Rol de la causa: 505-06 at §7.

²²⁶ *Energy Reserves Group v. Kansas Power & Light*, 459 U.S. 400, 411 (1983).

²²⁷ *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234 (1978).

²²⁸ *Id.* at 236-40.

Comparative Constitutional, *continued*

rendering the past contributions inadequate.²²⁹ The Court thus concluded that the law violated the Contract Clause.

Later, another important decision was *Energy Reserves Group, Inc. v. Kansas Power & Light Co.* (1983), which involved long-term contracts entered into for the sale by Energy Reserves Group (ERG) of natural gas to Kansas Power & Light. The contracts included clauses that permitted the prices to rise under certain circumstances. In 1979, the State of Kansas enacted price controls that prevented ERG from charging the higher prices that otherwise would have been allowed under the contract. ERG argued that the law violated the Contract Clause.²³⁰ The Supreme Court found that in light of the regulatory background of substantial and extensive regulation that existed when the contracts were entered into in 1975, ERG had no reasonable expectation that the price escalator clauses would not be affected by government regulation. Therefore, the Court concluded, there was no substantial impairment of ERG's contractual rights.²³¹

Federal courts have been quite creative in their interpretations of the Contract Clause while being mindful of the precedents laid down by the United States Supreme Court. For example, the Court of Appeals for the Fifth Circuit held in 2010 that “[Under the Contract Clause,] total destruction of contractual expectations is not necessary for a finding of substantial impairment.”²³²

Thus, the *substantiality* analysis pivots around ideas related to the importance or essence of the affected contract right,²³³ whether the exercise of the police power materially changes

the contractual terms,²³⁴ whether the contract changes are “of degree and not kind,”²³⁵ or whether police powers are exercised to tackle economic emergencies²³⁶ or crises,²³⁷ either permanent or temporary.²³⁸ Another important element is whether the sector of the economy in which the impairment occurs is “heavily regulated.”²³⁹ In this latter instance, the parties are deemed to have a less reasonable expectation that impairment would not take place.²⁴⁰

Perhaps the United States Court of Appeals for the Fourth Circuit best summarized the uncertainty of the *substantiality* analysis test when it opined in 1993 that:

The Supreme Court, however, has provided little specific guidance as to what constitutes a “substantial” contract impairment. It is clear that not all impairments are substantial

²³⁴ *Id.* at 898 (“Whether the Gas Company has suffered a substantial impairment turns on whether the exercise of the police power in this case materially changed the terms of the contract.”).

²³⁵ *Id.* at 895 (“Changed circumstances and important government goals do not make an impairment reasonable if the changed circumstances are ‘of degree and not kind.’”).

²³⁶ *Baltimore Teachers Union v. Mayor of Baltimore*, 6 F.3d 1012, 1015 (4th Cir. 1993) (“Analyzing Baltimore’s action within this framework, we agree with the district court that the City substantially impaired an extant contract with its teachers and police. We conclude, however, affording the requisite degree of deference to the City’s legislature, that the impairment was in exercise of the City’s legitimate powers and thus permissible under the Contract Clause.”).

²³⁷ *United Automobile v. Luis A. Fortuño*, 677 F.Supp.2d 530, 531 (D.P.R. 2009) (“The Court finds that the layoffs proposed by Law 7 are a cost-cutting and/or reorganization measure. As such, they fall under the reorganization exception....The layoffs are simply the method chosen by the government to solve the aforementioned financial crisis.”).

²³⁸ *Baltimore Teachers Union*, 6 F.3d at 1020 (“The public purpose justifying an impairment of contract need not be ‘an emergency or temporary situation,’ although the existence of an emergency is of course relevant.” (citing *Energy Reserves Group v. Kansas Power & Light*, 459 U.S. 400, 412 (1983)).)

²³⁹ *Campanelli v. Allstate Life Insurance Company*, 322 F.3d 1086, 1098 (9th Cir. 2003) (“The severity of the impairment is significantly mitigated, however, by the fact that the California insurance industry is heavily regulated.”). *See also Calfarm Ins. Co. v. Deukmejian*, 258 Cal.Rptr. 161, 771 P.2d, 1247, 1262 (1989) (“Insurance, moreover, is a highly regulated industry, and one in which further regulation can reasonably be anticipated.”).

²⁴⁰ *Id.*

²²⁹ *Id.* at 246-7.

²³⁰ *Energy Reserves Group*, 459 U.S. at 403-9.

²³¹ *Id.* at 413-6.

²³² *United Healthcare Insurance Co. v. Angele Davis*, 602 F.3d 618, 628 (5th Cir. 2010).

²³³ *Southern California Gas Company, v. City of Santa Ana*, 336 F.3d 885, 890 (9th Cir. 2003) (“An impairment of a public contract is substantial if it deprives a private party of an important right, [or] thwarts performance of an essential term, [or] defeats the expectations of the parties, [or] alters a financial term[.]”)

Comparative Constitutional, *continued*

for Contract Clause purposes. “Technical” impairments, for example, do not necessarily rise to the level of constitutional violations. *See id.* (“Minimal alteration of contractual obligations may end the inquiry at its first stage.”); *see also United States Trust*, 431 U.S. at 21, 97 S.Ct. at 1517 (“A finding that there has been a technical impairment is merely a preliminary step in resolving the more difficult question whether that impairment is permitted under the Constitution.”). By the same token, there is plainly no requirement of total repudiation. *See Energy Reserves [Group]*, 459 U.S. at 411, 103 S.Ct. at 704 (“Total destruction of contractual expectations is not necessary for a finding of substantial impairment.”); *United States Trust*, 431 U.S. at 26, 97 S.Ct. at 1519. The ground between these spectral ends, though, has yet to be charted with any precision.²⁴¹

In the case of Chile, the Constitutional Tribunal decided in 1982 one of the first cases explicitly applying article 19 §24 to contractual rights under the Chilean Constitution of 1980. Unlike *Allied Structural*, in the Chilean case the bill was aimed at reducing the size of government pensions for Chilean pensioners. The Tribunal declared the constitutionality of the bill based on the argument that adjustments of pension plans “were not a part of the right to social security in itself.”²⁴² In this way, the Tribunal analyzed the “essence” of contractual rights under the constitutional guarantee of property rights (*viz.*, the right to property), and determined that no “substantial” impairment existed for constitutional purposes.

7.4.3. Second Requirement: Significant and Legitimate Public Purpose

A significant and legitimate public purpose would usually occur when the measure is

passed to remedy a general social or economic problem, and not to benefit special interests.²⁴³ This key precedent was also reinforced in the case of *Allied Structural* (1978), in which the United States Supreme Court found that there was no showing that the “severe disruption of contractual expectations [retroactive increase in employee pension plans] was necessary to meet an important general social problem.”²⁴⁴ Later in 1983, in *Energy Reserves*, the Supreme Court ruled that Kansas’ price controls rested on significant and legitimate state interests in protecting consumers from price increases.²⁴⁵ In 2010, the Court of Appeals for the Fifth Circuit clarified that the exercise of a state’s police power needs to be aimed at “remediating a broad and general social problem”²⁴⁶ and not merely to serve “a narrow group or a special interest.”²⁴⁷

Other United States federal courts of appeals have mentioned other grounds for the admissibility of states’ police powers under the Contract Clause, such as “public welfare;”²⁴⁸ “a broad societal interest;”²⁴⁹ and “a broad and general social or economic problem.”²⁵⁰

²⁴³ *Id.* at 411-2.

²⁴⁴ *Id.* at 247.

²⁴⁵ *Id.* at 416-7.

²⁴⁶ *United Healthcare Insurance Co. v. Angele Davis*, 602 F.3d 618, 630 (5th Cir. 2010) (“To justify impairing a contract with the state, the law’s public purpose must be one that implicates the state’s police power, such as by remedying a ‘broad and general social problem[.]’ *Lipscomb*, 269 F.3d at 504-05. Providing a benefit to a narrow group or special interest is insufficient justification. *Id.*”).

²⁴⁷ *Id.*

²⁴⁸ *Campanelli v. Allstate Life Insurance Company*, 322 F.3d 1086, 1100 (9th Cir. 2003) (“Under the California Constitution, a statute can only be applied retroactively to impair vested rights if retroactive application ‘reasonably could be believed to be sufficiently necessary to the public welfare as to justify the impairment.’”).

²⁴⁹ *Equipment Manufacturers Institute v. Janklow*, 300 F.3d 842, 859 (8th Cir. 2002) (“Because a substantial impairment of pre-existing contractual rights exists, [the state] must demonstrate a significant and legitimate public purpose[.]”).

²⁵⁰ *Lipscomb, v. Columbus Municipal Separate School District*, 269 F.3d 494, 504 (5th Cir. 2001) (“A State can only justify a substantial impairment of contracts with a ‘significant and legitimate public purpose behind the regulation, such as the remedying of a broad and general social or economic problem[.]’ [citing *Energy Reserves Group v. Kansas Power & Light*, 459 U.S. 400, 412 (1983).] The problem need not be ‘an emergency or temporary situation,’ and ‘the elimination of unforeseen windfall profits’ is a legitimate state interest sufficient to justify state impairment of contracts.” [citing *Energy Reserves Group*, 459 U.S. at 412]).

²⁴¹ *Baltimore Teachers Union*, 6 F.3d at 1017.

²⁴² JORGE BARAHONA, *supra* note 26, at 57 (referring to *Rentas Vitalicias*, Rol de la causa: 334.).

Comparative Constitutional, *continued*

However and as a general rule, courts do exercise self-restraint on the topic of impairment of contracts by deferring to legislatures for the ultimate determination on when and how to exercise their police powers.²⁵¹ But, again, such deference is strongly limited when dealing with *public contracts*.²⁵²

In the case of Chilean jurisprudence, the test equivalent to the United States “significant and legitimate public purpose” is expressly established in the Constitution of 1980: article 24 § 19, authorizes the restriction of property rights under the concept of the “social function of property.” This latter notion, according to that provision, “includes all the requirements of the Nation’s general interests, the national security, public use and health, and the conservation of the environmental patrimony.” Chilean courts, accordingly, have interpreted the “significant and legitimate public purpose” expressly along the lines of the aforementioned language of article 24 § 19. More on the topic is reviewed in Section 8.2 *infra*.

7.4.4. Third Requirement: The Law or Regulation Must be a Reasonable and Appropriate Means to Achieve A Significant and Legitimate Public Purpose

To meet this requirement, United States courts treat government contracts differently from private contracts.²⁵³ With respect to general economic and social considerations, courts usually defer to legislative judgment as to the necessity and reasonableness of a particular action. Such deference has not been deemed to be appropriate when the state is a party to the contract in question, because the state’s self-

²⁵¹ *Baltimore Teachers Union v. Mayor of Baltimore*, 6 F.3d 1012, 1021 (4th Cir. 1993) (“The authority of the states to impair contracts, to be sure, must be constrained in some meaningful way. The Contract Clause, however, does not require the courts—even where public contracts have been impaired—to sit as superlegislatures[.]”).

²⁵² *Id.* at 1019 (“The Court has never expressly stated that any deference is owed legislative judgments in the context of public contract impairment. However, [this is] the most reasonable inference one gains from comparing its characterization in *United States Trust* of the deference due legislative judgments in the private contract context[.]”).

²⁵³ *Id.*

interest is at stake.²⁵⁴ In these cases, the state’s behavior is still subject to careful consideration by United States courts.²⁵⁵

The key case of *United States Trust Co. v. New Jersey*, decided by the Supreme Court in 1977, involved a New Jersey law passed during the energy crisis of 1974. The New Jersey law repealed a 1962 law that limited the extent to which the New York Port Authority subsidized rail passenger transportation. Port Authority bondholders argued that the 1974 repeal law violated the Contract Clause.²⁵⁶ Because this case involved a municipal bond contract, the Court declined to defer to the state legislature’s judgment of necessity and reasonableness.²⁵⁷ The Court found that the state had other alternatives available to meet its objectives, such as modifying (rather than repealing) the 1962 law or adopting alternative means of improving mass transit.²⁵⁸ It also noted that the repeal of the 1962 law could not be considered reasonable due to changed circumstances, because the state legislature in 1962 could have anticipated the likely future need for mass transit.²⁵⁹ The Court thus found the 1974 New Jersey law violated the Contract Clause.

Moreover, a year later in *Allied Structural*, the Supreme Court elaborated further that the law in question was not enacted to protect a broad societal interest, but rather had a very narrow focus, applying only to a small number of

²⁵⁴ *United States Trust Co. v. New Jersey*, 431 U.S. 1, 22-3 (1977). *See also* *United Healthcare Insurance Co. v. Angele Davis*, 602 F.3d 618, 627 (5th Cir. 2010) (“We do not defer completely to the legislature’s judgment because of the possibility that the state is acting in its own self interest regarding the contract.”).

²⁵⁵ *United Automobile v. Luis A. Fortuño*, 677 F.Supp.2d 530, 535 (D.P.R. 2009) (“[A] state must do more than mouth the vocabulary of the public weal in order to reach safe harbor; a vaguely worded or pretextual objective, or one that reasonably may be attained without substantially impairing the contract rights of private parties, will not serve to avoid the full impact of the Contracts Clause.”). *See also* *John J. Mascio v. Public Employees Retirement System of Ohio*, 160 F.3d 310, 314 (6th Cir. 1998) (“Where the state is a party to the contractual obligation in question, ‘complete deference to a legislative assessment of reasonableness and necessity is not appropriate because the State’s self-interest is at stake.’”).

²⁵⁶ *United States Trust Co.*, 431 U.S. at 4-14.

²⁵⁷ *Id.* at 24-5.

²⁵⁸ *Id.* at 30.

²⁵⁹ *Id.* at 31-2.

In both the United States and Chilean systems, jurisprudence broadly recognizes the role of contracts as an essential element of societal life.

Comparative Constitutional, *continued*

employers²⁶⁰ [retroactive increase in employee pension plans], and therefore did not meet the reasonableness test. In 1983, in the case of *Energy Reserves*, the Supreme Court ruled that the means used by the state to achieve its goals were reasonable,²⁶¹ and consequently rejected ERG's claim that the Kansas law violated the Contract Clause.

Federal appellate courts throughout the country have broadly followed the reasonableness and appropriateness standards established by the Supreme Court in *United States Trust Co.* and *Allied Structural*.²⁶² Furthermore, after the aforementioned controlling decisions of the Supreme Court, federal circuit courts of appeals have become increasingly stringent in their requirement of "severity" to determine the unreasonableness of the contract impairment.²⁶³ In this vein, for instance, in 2011 the United States Court of Appeals for the First Circuit strongly upheld this constraint, calling it "a critical inquiry."²⁶⁴

8. Exceptions to the Constitutional Protection of Contracts in Both the American and Chilean Systems

²⁶⁰ See generally *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 248-250 (1977).

²⁶¹ See generally *Energy Reserves Group v. Kansas Power & Light*, 459 U.S. 400, 418-9 (1982).

²⁶² *Pendergraph v. North Carolina Department of Revenue*, 2011 WL 1678063, *3 (N.C. Super. 2011) (Unpublished opinion) ("It is well settled in North Carolina that employees whose rights in the retirement system have vested have a relationship with the State that is contractual, and absent an important interest that is reasonable and necessary, the State cannot impair this right."). See also *United Healthcare Insurance Co. v. Angele Davis*, 602 F.3d 618, 627 (5th Cir. 2010) ("An important consideration in our substantial impairment analysis [under the Contract Clause] is the extent to which the law upsets the reasonable expectations the parties had at the time of contracting, regarding the specific contractual rights the state's action allegedly impairs.").

²⁶³ *United Automobile v. Luis Fortuño*, 633 F.3d 37, 48 (1st Cir. 2011) ("One reason why plaintiff victories are rare is that courts are not in a good position to determine the unreasonableness of the impairment unless it is particularly severe.").

²⁶⁴ *Id.* at 45 ("Even though we assume arguendo that there was an impairment, and that the impairment was substantial, ascertaining the severity of the impairment is still a critical inquiry in determining whether a state action is a reasonable means of advancing a public purpose."). See *Energy Reserves Group v. Kansas Power & Light*, 459 U.S. 400, 411 (1983). ("The severity of the impairment is said to increase the level of scrutiny to which the legislation will be subjected.").

8.1. United States "Police Powers" as a Restriction to Constitutional Protection of Contracts

Many States' constitutions contain a Contract Clause mirroring that of the United States Constitution, and typically the States' highest courts interpret their own Contract Clauses along the lines of the United States Supreme Court's interpretations.²⁶⁵

Historically, United States Courts recognized early on the restrictions placed by Natural Law on States' police powers to adopt legislation aimed at protecting "public health, safety, morals,²⁶⁶ and welfare generally."²⁶⁷ Nonetheless, there was countervailing consideration that the Contract Clause had not established a blanket prohibition of the States for intervening in private contracts. Accordingly, several decisions held that the very existence of the States depended on the extent of their powers over private citizens. Thus, it was sustained that states could not "contract away their power of eminent domain, or their police power, nor any of their power to supervise and regulate the forms of administering justice ... [and that they could not] contract concerning governmental subjects."²⁶⁸ It was also expressed that there was "no contract between the state and its citizens as to what taxes shall be imposed[.]"²⁶⁹

Despite the strong language of the restrictions invoked by United States courts over contractual freedom, some United States courts have repeatedly and consistently held that State supremacy powers must be "exerted for the

²⁶⁵ *Montague v. Dixie National Life Insurance Company*, 2011 WL 2294146 at *8 (D.S.C. 2011). ("South Carolina's Constitution also contains a Contract Clause, which bars the State from passing laws that impair the obligations of contracts, S.C. Const. art. I, § 4, and the South Carolina Supreme Court has followed federal precedent construing the federal Contract Clause in interpreting the Contract Clause of the South Carolina Constitution.").

²⁶⁶ PAGE, *supra* note 15, at 2405.

²⁶⁷ Ethan Shenkman, *Could Principles of Fifth Amendment Takings Jurisprudence Be Helpful in Analyzing Regulatory Expropriation Claims Under International Law?* 11 N.Y.U. ENVTL. L.J. 174, 187 (2002-2003).

²⁶⁸ HUNTING, *supra* note 7, at 52 (citing *Stone v. Mississippi*, 101 U.S. 814 (1879)).

²⁶⁹ BLACK, *supra* note 4, at 726.

Comparative Constitutional, *continued*

common good and welfare[.]”²⁷⁰ As a result, provisions in charters or statutes in which a State “barter[s] away its powers of sovereignty, such as the police power, the power of taxation or the power of eminent domain” were considered null and void.²⁷¹ But at any rate, the determination of the legitimacy of state powers is a matter of federal and not state law.²⁷²

8.2. The “Social Function of Property” as a Restriction of Contractual Rights in Chile

In the case of Chile, courts have recognized that the Constitution of 1980 established a delicate balance between legitimate public interests and the defense of private property.²⁷³ In effect, the Chilean Supreme Court has interpreted the constitutional rule on the *intangibilidad* of contracts not as an absolute norm devoid of exceptions. Quite the opposite, that Court has held that private property must not be made to further arbitrariness.²⁷⁴ It has also recognized that “[T]he fact that a right originates in a private contract and not in a law”²⁷⁵ does not constitute an obstacle to determining, according to the Constitution, that restrictions may be imposed based on the notion of the social function of the property, and based on national or public interest. Consistent with this, the same Court held in 2007 that,

To sustain the absolute *intangibilidad* of the rights arising from contracts not only lacks a constitutional foundation, but would require to sustain as constitutionally permitted countless

²⁷⁰ *Id.* at 727.

²⁷¹ DONNELLY, *supra* note 138, at 133.

²⁷² *Lipscomb v. Columbus Municipal Separate School District*, 269 F.3d 494, 512 (5th Cir. 2001) (“[W]hether state powers are legitimate justifications for impairment of contracts is a question of federal, not state, law.”).

²⁷³ *Transelec*, Rol de la causa: 505-06 at § 17.

²⁷⁴ Decision of the Chilean Constitutional Tribunal on Catalytic Vehicles, Case No. 325 (Unconstitutionality Writ Submitted by Several Senators for the Tribunal to Resolve the Constitutionality of Supreme Decree No. 20 of the Ministry of the General Secretariat of the Presidency of January 22, 2001, published in the *Diario Oficial* [Official Gazette] on April 12, 2001, According to Article 82, No. 5, of the Political Constitution of the Republic (Santiago, June 26, 2001)).

²⁷⁵ *Transelec*, Rol de la causa: 505-06 at § 19.

usual practices in our legal system, such as that of granting, by law, new labor or social security benefits to workers payable by their employers.²⁷⁶

In this sense, the Chilean Constitution of 1980 created a unique restriction on property rights. In fact, article 19 §24 provides, in part, that “[O]nly the law may establish the ... limitations and obligations derived from [the property’s] social function.” This constitutional provision has been repeatedly ratified by the Chilean Constitutional Tribunal, which in 2006 sustained that “there is nothing in the nature of the right to property over incorporeal things prohibiting to limit them based on the social function of property.”²⁷⁷

The remote source of the social function restriction is found in the Scholastic writings of Catholic theologians and canon lawyers, who sought to moralize contracts²⁷⁸ beyond the strictness of the Roman Law concept of contract. This way, the Social Doctrine of the Catholic Church served as the moral background for the constitutional design of the notion of the “social function” of the property. As a scholar notes,

[I]f we analyze the political-ideological aspects regarding ownership within the last 20 or 30 years in our country [Chile], we find that most of them are inspired by the emphasis on the essential teachings of the Social Doctrine of the [Catholic] Church. While socialistic theories have placed greater emphasis on the concept of ‘social function’ proposed by the doctrine, more traditional groups have emphasized the recognition and protection of the right of the owner.²⁷⁹

The Chilean constitutional provisions authorizing limitations to the right to property distinguish between “limitations and

²⁷⁶ *Id.* at § 18.

²⁷⁷ *Id.* at § 17.

²⁷⁸ JORGE LÓPEZ, *supra* note 30, at 260-1 (referring to Saint Thomas of Aquinas in particular).

²⁷⁹ ARTURO FERNANDOIS, *supra* note 19, at 260.

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obligations” imposed over private property that trigger the government’s obligation to compensate the owner, from those which do not.²⁸⁰ As the Chilean Supreme Court has stated, the difference resides in whether such “limitations and obligations” imposed by the law affect the essence of the right to property, with measures that might:

[D]eny or severely curtail the right to use, to enjoy, or to dispose of the property, restricting some of these attributes with measures such that the owner becomes a dependent of the public authority [or] deprive [him] of the ability to manage [thus arriving at] the effective deprivation of property or any of its three attributes, as a result of acts of authority not accepted or condoned by the owners, and that are not included in the legal rights that form the social function of property.²⁸¹

On the other hand, in 2004 the Chilean Supreme Court interpreted the concept of the “general interests of the Nation” to uphold a law imposing restrictions on private property based on its declaration as a “Historic Monument,” and rejecting the claims of the private party.²⁸² In the same decision the Court affirmed that the notion of “general interests of the Nation” “cannot become so protean as to fit all of the restrictions that the legislature wants to impose on the property.”²⁸³ The Court further added that:

[T]he general interests of the Nation expresses a legal right that is directly related to the entire Nation, as a whole, and never, however important, with a section of it, and that relates basically to the greater benefit of the global political society as a whole, without reference to

social categories or groups, economic or of other nature.²⁸⁴

However, the Chilean Supreme Court has understood that these exceptions “must always be interpreted and applied restrictively.”²⁸⁵ Yet in 2004, the Supreme Court affirmed that the legislature may never, “without legal objection, take refuge in a pretended general interest in order to tax private property with restrictions or obligations that the Constitution of 1980 specifically authorized only in very exceptional situations.”²⁸⁶

Conclusion

Our analysis has sought to identify the areas where the constitutional doctrines of impairment of contracts and *intangibilidad* of contracts converge and diverge in both constitutional systems. Not to our surprise, the points of similarity are more numerous than not. This article has shown how the constitutional history and current constitutional framework of the United States and Chile share in the common tradition of the Western legal world concerning the respect and protection of contracts. In effect, the United States, from the outset of its existence, through the vigorous jurisprudence of United States Supreme Court Chief Justice John Marshall and Associate Justice Joseph Story, has seen its Supreme Court take an active role in shaping a solid defense of private initiative and contractual rights. Admittedly, this approach underwent changes during the antebellum and postbellum Civil War era, as well as during the period of the New Deal.

In the case of Chile, the Chilean Supreme Court articulated very early its defense of the *intangibilidad* of contracts, and contributed this jurisprudence to Chile’s early constitutional development. In the twentieth century, during the late sixties and early seventies, setbacks occurred affecting the firmness of the doctrine,

²⁸⁰ *Transelec*, Rol de la causa: 505-06 at § 6 (“A law affecting the attributes that the owner has over the object of his property entails impairing the essence of the contract, and therefore, constitutes an expropriation of such property that constitutionally must be compensated for by the State.”).

²⁸¹ *Inmobiliaria Maullín Limitada*, Rol de la causa: 4-309 at 215§ 6, ¶ 2.

²⁸² *Id.* Dissenting opinion, § 6.

²⁸³ *Id.* § 6 ¶ 3.

²⁸⁴ *Rentas Vitalicias*, Rol de la causa: 334 at § 22.

²⁸⁵ Miguel Fernández, *supra* note 173, at 29.

²⁸⁶ *Inmobiliaria Maullín Limitada*, Rol de la causa: 4-309 at § 6, ¶ 3.

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but the trend during the last thirty years under the Constitution of 1980 has been clearly on the side of its support.

The traditional Chilean approach to the protection of property rights before regulatory changes is based on the French distinction between “consolidated rights” and “mere expectations.” The effect of this criterion is more rhetorical than real. For this reason, as of late, the Chilean Constitutional Tribunal has looked to other different doctrinal sources developed within Chilean and comparative constitutional literature. It is in this context that the Chilean Constitutional Tribunal, and sometimes ordinary Chilean courts, have used the “essential content” principle, the “legitimate expectations” principle, and the proportionality test, which has already been reviewed.

To conclude, in both the United States and Chilean systems, jurisprudence broadly recognizes the role of contracts as an essential element of societal life, but also preserves the power of “the State” (in Chile, the unitary state; in the United States, both the federal government and the constituent states) to regulate private affairs in order to protect the public interest. In both the United States and Chile these restrictions have been interpreted with an aim to restrict retroactivity and to protect a private party’s reasonable expectations. Ultimately, the concepts of “police powers,” or “social function of property” may yet be the subject of novel interpretations, but retain different degrees of restricted application in both systems.



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