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Opinion No. 10-14

Vendors' Contractual Rights Under the State and Federal Constitutions

QUESTION

May the General Assembly constitutionally require that, as a condition to contracting with a state agency or political subdivision, a vendor of goods or services involving surveillance cameras operated in accordance with Tenn. Code Ann. § 55-8-198 hereafter agree to incorporate into any such contract any subsequently enacted changes to that statute, thereby waiving the vendor's rights under the Contract Clauses of the Federal Constitution, Article I, Section 10, and the Tennessee Constitution, Article I, Section 20; or, would such a requirement violate the "unconstitutional conditions" doctrine?

OPINION

The General Assembly may constitutionally require that, as a condition to contracting with a state agency or political subdivision, a vendor of goods or services involving surveillance cameras operated in accordance with Tenn. Code Ann. § 55-8-198 must agree to incorporate into any such contract any subsequently enacted changes to that statute; provided, however, any terms that are incorporated into an existing contract due to statutory changes must be reasonable. A court would be unlikely to permit enforcement of completely unforeseeable and/or unreasonable terms inserted into an existing contract, and such terms would be subject to an attack on the basis of unconscionability.

ANALYSIS

Article I, Section 20, of the Tennessee Constitution provides "[t]hat no retrospective law, or law impairing the obligations of contracts, shall be made." The Constitution of the United States, Article I, Section 10, also prohibits any state from passing any law impairing the obligation of contracts. The Tennessee Supreme Court has stated that the meanings of the federal and state constitutional provisions are identical. *First Utility District of Carter County v. Clark*, 834 S.W.2d 283, 287 (Tenn. 1992); *Paine v. Fox*, 172 Tenn. 290, 112 S.W.2d 1 (Tenn. 1938).

Article I, Section 20, of the Tennessee Constitution prohibits laws which take away or impair vested rights acquired under existing laws or create a new obligation, impose a new duty, or attach a new disability in respect of transactions or considerations already passed. *Doe v. Sundquist*, 2 S.W.3d 919, 923 (Tenn. 1999) (quoting *Morris v. Gross*, 572 S.W.2d 902 (Tenn.

1978)). Among the primary tests for whether the obligation of a contract has been impaired are whether the value of the contract or security has been lessened, *Lake County v. Morris*, 160 Tenn. 619, 28 S.W.2d 351 (1930), or whether the right in full existing at the time the contract was executed has been diminished. *Hannum v. McInturf*, 65 Tenn. 225 (1873). The laws affecting enforcement of a contract, and existing at the time and place of its execution, enter into and form a part of that contract. *Kee v. Shelter Insurance*, 852 S.W.2d 226, 228 (Tenn. 1993). In that case, the Tennessee Supreme Court found that an extension in the statute of limitations could not constitutionally apply to a claim that had already accrued under an insurance contract before the extension was passed.

Your question suggests a scenario whereby a vendor of surveillance camera services or goods would be required, as a condition of contracting with the State or a local government, to agree in advance to incorporate into the contract any future amendments to Tenn. Code Ann. § 55-8-198. That is, the original contract would contain a provision binding the vendor to compliance with any future statutory changes regarding surveillance camera goods or services.

In determining whether a particular state regulatory measure (in this case, future amendments to Tenn. Code Ann. § 55-8-198 that are presently unknown) is constitutionally valid under the federal Contract Clause, federal courts generally apply a three-pronged test. *Energy Reserves Group, Inc. v. Kansas Power & Light Co.*, 459 U.S. 400, 410-13, 103 S.Ct. 697, 704-05, 74 L.Ed.2d 569, 580-81 (1983). The threshold inquiry is whether the state law has, in fact, operated as a substantial impairment of a contractual relationship. *Allied Structural Steel Co. v. Spannaus*, 428 U.S. 234, 244, 98 S.Ct. 2716, 2722, 57 L.Ed.2d 727 (1978). In determining the extent of the impairment, the courts are to consider whether the industry the complaining party is engaged in has been regulated in the past. *Id.* at 242 n.13, 98 S.Ct. at 2721 n.13. Where, in light of all facts and circumstances, including past regulation and the terms of the agreement, a change in state law is foreseeable, the change does not impair the parties' reasonable expectations. *Energy Reserves Group*, 459 U.S. at 710, 103 S.Ct. at 707, 74 L.Ed.2d 569. The Tennessee Supreme Court relied on similar factors to determine whether a change in the process of accessing adoption records impaired a "vested right" in violation of Article I, Section 20, of the Tennessee Constitution. *Doe*, 2 S.W.3d at 924. The Court inquired, first, whether the public interest is advanced or retarded; second, whether the retroactive provision gives effect to or defeats the *bona fide* intentions or reasonable expectations of the affected persons; third, whether the statute surprises persons who have long relied on a contrary state of the law; and finally, the extent to which a statute appears to be procedural or remedial.

Because your question concerns the application of future statutory changes that are currently unknown, it is impossible to provide a meaningful analysis applying these legal principles to the facts. The first question, however, would likely be whether, in light of all the facts and circumstances, the change in the law would be a substantial impairment of a contractual relationship between the State or local government and the vendor of surveillance camera goods or services.

Under the federal Contract Clause, if the challenged regulatory measure does impair a contract, then the second inquiry is whether the regulatory measure came into being pursuant to a

significant and legitimate public purpose, *United States Trust Co. v. New Jersey*, 431 U.S. 1, 22, 97 S.Ct. 1505, 1517, 52 L.Ed.2d 92 (1977), such as the remedying of a broad and general social or economic problem. *Allied Structural Steel Co.*, 428 U.S. at 247, 249, 98 S.Ct. at 2723-25. Once a legitimate public purpose has been identified, the next inquiry is whether the adjustment of “the rights and responsibilities of contracting parties [is based] upon reasonable conditions and [is] of a character appropriate to the public purposes justifying [the legislation] adoption.” *United States Trust Co.*, 431 U.S. at 22, 97 S.Ct. at 1518. Furthermore, as is customary in reviewing economic and social regulation, . . . courts properly defer to legislative judgment as to the necessity and reasonableness of a particular measure. *Energy Reserves Group*, 459 U.S. at 412-13, 103 S.Ct. at 704-05, 74 L.Ed.2d at 581.

The next question, therefore, would be whether the statutory change came into being pursuant to a significant and legitimate public purpose, such as the remedying of a broad and general social or economic problem. Assuming this question is answered in the affirmative, the question then becomes whether the adjustment of the rights and responsibilities of the parties to the contract is based upon reasonable conditions and is of a character appropriate to the public purposes justifying the extension.

It must be noted that a contract provision requiring compliance with as-yet-unknown terms and conditions would not necessarily violate the constitutional “impairment of contracts” clauses because the vendor, in agreeing to such a contract provision, would be doing so with the knowledge that future statutory amendments would be incorporated into the existing contract.¹ It is therefore vital to distinguish between the current contract provision making future amendments applicable and binding, and the as-yet-unknown future changes to both the statute and the existing contract. Where a contractor agrees in advance to be bound by unknown future terms and conditions, a court might not consider those future changes “impairment of existing contract rights,” since the parties agreed in advance to be bound. Rather, where the contractor agreed in advance to future changes, the future changes would likely be deemed new terms that had been mutually anticipated by the parties to the original contract.

Any new contract terms imposed by subsequent statutory changes on a contract would be subject, however, to a “reasonableness” analysis, and the contractor/vendor might attack unreasonable terms as unconscionable, and thus unenforceable.

The question of whether a contract or provision thereof is unconscionable is a question of law. *See Lewis Refrigeration Co. v. Sawyer Fruit, Vegetable & Cold Storage Co.*, 709 F.2d 427, 435 n. 12 (6th Cir.1983).

If a contract or term thereof is unconscionable at the time the contract is made, a court may refuse to enforce the contract, or may enforce the remainder of the contract without the unconscionable term. *See Restatement (Second) of Contracts § 208 (1981).* “The determination that a contract or term is or is not unconscionable is made in the light of its setting, purpose and effect. Relevant

¹It is common for contracts to require compliance with applicable federal and state laws, rules, and regulations, including changes and amendments thereto made subsequent to the execution of the contract.

factors include weaknesses in the contracting process like those involved in more specific rules as to contractual capacity, fraud, and other invalidating causes . . . ” Restatement (Second) of Contract § 208, cmt. a (1981).

Enforcement of a contract is generally refused on grounds of unconscionability where the “inequality of the bargain is so manifest as to shock the judgment of a person of common sense, and where the terms are so oppressive that no reasonable person would make them on the one hand, and no honest and fair person would accept them on the other.” *Haun v. King*, 690 S.W.2d 869, 872 (Tenn.Ct.App.1984) (quoting *In re Friedman*, 64 A.D.2d 70, 407 N.Y.S.2d 999 (1978)); *see also Aquascene, Inc. v. Noritsu Am. Corp.*, 831 F.Supp. 602 (M.D.Tenn.1993). An unconscionable contract is one in which the provisions are so one-sided, in view of all the facts and circumstances, that the contracting party is denied any opportunity for meaningful choice. *Id.*

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The contract signed between Taylor and City Auto is one of adhesion, in that it is a standardized contract form that was offered on essentially a “take it or leave it” basis without affording Taylor a realistic opportunity to bargain. *See Black’s Law Dictionary* 40 (6th ed. 1990). We have previously determined that enforceability of contracts of adhesion generally depends upon whether the terms of the contract are beyond the reasonable expectations of an ordinary person, or oppressive or unconscionable. *See Buraczynski v. Eyring*, 919 S.W.2d 314, 320 (Tenn.1996). Courts will not enforce adhesion contracts which are oppressive to the weaker party or which serve to limit the obligations and liability of the stronger party. *Id.*

Taylor v. Butler, 142 S.W.3d 277, 284-86 (Tenn. 2004).

Thus, for example, if a surveillance camera vendor were to sign a five-year contract with a local government under a contract providing that subsequent changes to Tenn. Code Ann. § 55-8-198 were to be incorporated into the contract and become binding on the parties, and two years later Tenn. Code Ann. § 55-8-198 was amended to require the use of updated software that was readily available in the industry, this change would likely be enforceable, all other things being equal. On the other hand, if the amendment to Tenn. Code Ann. § 55-8-198 provided that vendors would henceforth be paid a substantially lower amount for their services than had originally been provided for in the contract, a reviewing court would be unlikely to find such a change reasonable or enforceable.

Accordingly, it appears that the General Assembly may constitutionally require that, as a condition to contracting with a state agency or political subdivision, a vendor of goods or services involving surveillance cameras operated in accordance with Tenn. Code Ann. § 55-8-198 must agree to incorporate into any such contract any subsequently enacted changes to that statute. This is subject to the proviso, however, that any future statutory changes that are incorporated into the existing contract must be reasonable. A court would be unlikely to permit enforcement of

completely unforeseeable and/or unreasonable terms into an existing contract, and such terms would be subject to an attack on the basis of unconscionability.

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