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The topic of this discussion is unconstitutional conditions. I have written a book, *Bargaining with the State*,[1] which discusses the topic. However, Judge Randolph's brief introduction has raised a number of questions I have not thought about at all. This proves how rich, complicated, and convoluted the subject is. In this short talk, I will take refuge in a safe harbor open to all academics, and discuss the basic theory of the subject. My speech will be in the form of a political and intellectual puzzle that urgently requires some principled resolution.

The doctrine of unconstitutional conditions asks whether or not the government may attach certain conditions — the potential range is well-nigh infinite — to particular grants or contracts. If you look at recent cases on that subject, you will discover immediately that squarely and staunchly in the freedom of contract camp is a notable market economy stalwart Justice William J. Brennan. If, for example, you read his *Nollan* dissent,[2] you will discover that if the government can stop a new development from proceeding, it may certainly condition the grant of the requisite permits on the surrender of a lateral easement across the front of the property. After all, Brennan asserts, you could always reject the deal and lose nothing you already have, or you can accept the bargain which will both be in your interest and the state's interest. The entire transaction exhibits the gains from trade that conservative economists praise. According to Justice Brennan, under the circumstances, it was perfectly appropriate for the state to impose a condition on the permit power grant.

Brennan's challenge is this: why is it strong believers in the scope of both federal and state power are also ardent champions of the doctrine of freedom of contract when the government is a party to the transaction? Why would they take that position when similar transactions made by private parties would be considered instruments of exploitation and advantage?

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[1] RICHARD A. EPSTEIN, BARGAINING WITH THE STATE (1993).

[2] Nollan v. California Coastal Comm'n, 483 U.S. 825, 842 (1987) (Brennan, J., dissenting).

I am an equal opportunity critic. Therefore, I must criticize the opposing argument. There are conservative justices who are deeply supportive of freedom of contract in market settings, but who become profoundly suspicious of its logic when the transactions have government as a party. Just as Justice Brennan wrote the dissent in *Nollan*, Justice Scalia graced us with his court opinion holding the "greater" power to exclude new construction did not carry with it the "lesser" power to permit that new construction upon the easement's surrender.[3] Judges who do not like discussing exploitation, extortion, inequality of bargaining power, or abusive exchanges in the private sector curiously adopt this logic in cases where government contracts resemble voluntary transactions. So "who's on first"? What's going on here? How are we going to resolve this mess? Is there something in this debate that makes sense, or is it a question of simple intellectual opportunism on all sides?

This problem is of special importance to me because I, for these purposes, fall underneath the broad umbrella of conservatism. Though I am not a Republican, no one would ever mistake me for a Democrat, particularly regarding domestic issues relating to government regulation and taxation. The difficulty is how to decide who is correct and who is incorrect for at least part of the time.

I think the point of departure for this discussion is to look for close private analogies to public transactions. There is a two-tier understanding of contract that proves helpful here. At stage one, it is very easy to understand there are all sorts of rules that prohibit fraud, that prohibit a duress, and that protect the insane and incompetent. However, at stage two which travels beyond these clear cases, there is another private contract law strand which discusses bargaining power inequalities without opening up the world to the New Deal state. Thus, there are particular rules dealing with contracts for marine salvage, or other transactions entered into under conditions of necessity, or under circumstances where one person is under immediate danger to lose life and limb.

These necessity situations all involve monopoly situations, or more precisely, bilateral monopoly situations. In those contexts, even on the private side, freedom of contract will not be fully operative. The persons who extract large sums of money to provide what would be (absent their monopoly posi-

[3] *Id.*

tion) routine, ordinary services, will find their bargains are not enforced. They will not, however, leave the table uncompensated, nor will they be in a worse position than their pre-transaction state. Instead, they will be limited to some just rate of return on the property and labor they committed to the particular venture. These are cases of just compensation and are not cases of total contractual invalidity. To the common lawyer, ordinary property rights are suspended under conditions of necessity. To the economist, everyone is in a better position if they are forced to commit to a system of competitive pricing in advance, notwithstanding momentary, transient pockets of monopoly power.

This view of the world should provide us with an important clue to understanding the bargaining process with the state. The government does not have transient monopolies such as those given to the dock owner in the great case of *Vincent v. Lake Erie Transportation Co.*[4] When the issue is permits and licenses, the government has a permanent monopoly presence which must be constitutionally neutralized if citizens are to be able to deal on a level playing field, and if government conduct is to be properly constrained. The issue is not any particular exchange's mutual gain, which is Justin Brennan's exclusive concern, but is instead the long-term governments' incentives to establish certain patterns of behavior, secure in the knowledge they will have enormous leverage against citizens.

That concern expresses itself in two ways. First, suppose I happen to steal your watch and then offer to sell it back to you. That second transaction is surely a slight improvement over the prior state of the world in which I keep your watch and you keep your money. However, if we allow the thief to resell the stolen goods, we induce a higher initial level of theft. It is easy to see why we place prohibitions on the second transaction to reduce the first transaction's (the theft's) probability of occurring.

Surprisingly, in the unconstitutional concerns areas, the Government is often in the business of taking. Accordingly, everyone should be desperately concerned that the Government will take things with one hand, and then, with the other hand, sell these things back to individuals (or in a federal system, the

[4] 124 N.W. 221 (Minn. 1910) (Boat owner who moored his vessel at a private dock during a storm was required to pay dock owner for damages to dock caused by boat).

states) with conditions imposed upon the individuals which the Government could never have directly imposed.

This is what I call the twin perils in bargaining with the state: the bargaining risks associated with bi-lateral monopoly, and the taking associated with taxation. Therefore, a sensible view of freedom of contract in the private arena should transfer to the public arena. It explains why the Government should be under greater scrutiny when contracting than the scrutiny ordinary, private individuals receive. Government's coercive power and its monopoly position often are creatures of statutes. Thus, its bargains should be carefully scrutinized. After having stated that basic proposition, I can now address the unconstitutional conditions paradox at a highly theoretical level and can attempt to resolve it.

The proper approach is this: in the usual situation, we can assume each party's position *ex post* is better than its *ex ante* position. Thus, there is nothing about which to complain. Under this standard, Justice Brennan is correct when he insists anybody who capitulates to a Government demand in a permit struggle is in a better position after receiving the permit, even though that party had to surrender an easement over his property. However, using a different perspective, we should ask ourselves: what would be the result if the bargain proceeded without the condition? Would that position be preferable to proceeding with the condition or preferable to having no bargain? When state transactions impose a monopoly power risk, a world without some particular condition will, on balance, produce greater net worth than a world subject to that condition.[5] If this is true, we have the familiar baseline problem: do we treat the baseline by which we judge gains and losses as the *status quo ante*, or do we treat it as the hypothetical optimal bargain world with bargains *sans* conditions?

Viewing the world through this lens, it is quickly apparent that certain conditional bargains, when examined for their substantive effect, will be wealth-destroying relative to unconditional bargains. Other conditional bargains will be wealth-enhancing and should be allowed. However, when the conditions are wealth-destroying conditions, we are confident that the state is in a better position when the transaction is unconditional, than when the transaction is never completed. Therefore,

[5] For numerical examples of the various permutations, *see* RICHARD A. EPSTEIN, BARGAINING WITH THE STATE *supra* note 1, at 99.

the condition should be eliminated for social welfare reasons. The question is how to identify which kinds of conditions are bad and which kinds of conditions are good. The constitutional question is to find a means to address these concerns.

Here are a few easy examples. First, suppose that a party who wants to use the public highways of a particular state must agree to submit to that state's jurisdiction if any traffic accident occurs in that jurisdiction. In 1925, when the Massachusetts Supreme Judicial Court faced that question, it gave the usual "bitter with the sweet" rationale and stated that this condition was perfectly appropriate.[6] That result was reached by a court which believed in the necessity of taking the "bitter with the sweet". This rationale is too broad because it allows any condition to be attached to private use of the public roads. However, it appears both sides are in better positions because they have prompt resolutions of their dispute. Therefore, that condition should be considered wealth-enhancing.

Second, suppose the state says: you may use the public highways only if you agree to be regulated as a common carrier. In addition, we will set minimum monopoly prices for your services. That condition pulls us away from the competitive equilibrium and should be struck down. It was struck down in one case,[7] but upheld in another case.[8]

Third, though economic liberty issues are not strong arguments today, however, the doctrine of unconstitutional conditions still survives. This doctrine allows the state to say: you may use the public highways only if you sacrifice your First Amendment rights, agree to pay dues to a religious organization not of your own choosing, or vote for the dominant political party in the next election. Justice Brennan would have joined with Justice Scalia to strike down these conditions. It is important to ask, what is going on under these circumstances? We cannot understand how the operation of the highways will be improved by these types of collateral conditions. As expected,

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[6] *In re* Opinion of the Justices, 147 N.E. 681 (Mass. 1925).

[7] Frost & Frost Trucking Co. v. California Railroad Comm'n, 271 U.S. 583 (1926) (private carrier who faced revocation of business license if he failed to get permit to use public highways was found to have been deprived of his property without due process of law).

[8] Stephenson v. Binford, 287 U.S. 251 (1932) (Texas practice of charging rates to common carriers to use public highways and charging private carriers the same or greater rate was neither a taking nor an interference with contract).

these are exactly the types of conditions courts have systematically struck down. It does not matter that the "bitter with the sweet" rhetoric applies to all cases, regardless of the condition's content.

In these hypothetical situations, there is a broad jurisprudential issue. Though one might want to swallow the bitter (in order to gain the sweet) and invoke the Hobbesian injunction that the content of a given transaction should be left to the appetite of the parties who know their own interests, it is not a rational position. It is no longer possible to state that parties make contracts and the state enforces them, because some knowledge of market conditions is necessary. Where monopoly power lodges in the government, a substantive examination of the contract for constitutional challenges is strictly necessary before its terms are upheld. The bargaining risks and the takings risks are too pervasive to be overlooked or ignored when the government is involved.

Of course, working with this doctrine is not easy. It is still necessary to determine which level of scrutiny should be brought to any examination of government activities. The government does not own a "free pass" to confiscate. The courts must delineate limits on state power. Yet, the solution to the first difficulty immediately raises a second difficulty: to what extent can we expect judges to respect the fine-spun distinctions in this area? Our next speaker, Judge Steven Williams does not believe that it is possible his colleagues on the bench can negotiate the pitfalls of this doctrine. He thinks a passive approach is better than the mischief theorists, like myself, are all too eager to create. I disagree with him. The Supreme Court often does its best when it tries its hardest. It only tries its hardest when it believes there is some abuse of the political process that it should correct. The stark abuse of power cases using strings and conditional grants should spur the Court to greater action, and should spur Judge Williams and his colleagues to perform at the high judicial diligence level we expect from them. In principle, we can resolve the puzzle of the doctrine of unconstitutional conditions. However, it requires judges with courage and intelligence to make sure we do not lose our way in our constant effort to use responsible judicial behavior to combat legislative excesses.