IN THE SUPREME COURT

STATE OF ARIZONA

JIE CAO, et al., Plaintiffs/Appellants, v. PFP DORSEY INVESTMENTS, LLC, et al., Defendants/Appellees.	Supreme Court No. CV-22-0228-PR Court of Appeals Division One Case No. 1 CA-CV 21-0275 Maricopa County Superior Court No. CV2019-055353

BRIEF AMICUS CURIAE OF GOLDWATER INSTITUTE IN SUPPORT OF PETITION FOR REVIEW FILED WITH CONSENT OF ALL PARTIES

Timothy Sandefur (033670)
Scharf-Norton Center for Constitutional Litigation at the GOLDWATER INSTITUTE
500 E. Coronado Rd.
Phoenix, Arizona 85004
(602) 462-5000
Litigation@goldwaterinstitute.org
Counsel for Amicus Curiae Goldwater Institute

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IDENTITY AND INTEREST OF AMICUS CURIAE

The Goldwater Institute is a public policy foundation dedicated to advancing the principles of individual liberty and limited government. Through its Scharf-Norton Center for Constitutional Litigation, the Institute often represents parties in cases challenging unconstitutional government actions—including situations where, as in this case, the unconstitutional action is embedded in a contract. *See, e.g.*, *Schires v. Carlat*, 250 Ariz. 371 (2021); *Cheatham v. DiCiccio*, 240 Ariz. 314 (2016); *Savas v. Cal. State Law Enf't Agency*, No. 22-212, (U.S. filed Sept. 8, 2022). The Institute has often been involved in lawsuits in which government entities seek to insulate unconstitutional actions from review by characterizing them as consensual agreements. *See, e.g., id.*; *Belgau v. Inslee*, 975 F.3d 940 (9th Cir. 2020), *cert. denied*, 141 S. Ct. 2795 (2021); *Janus v. AFSCME*, 141 S. Ct. 1282 (2021). The Institute believes its policy expertise and experience will aid this Court in considering this petition.

INTRODUCTION AND SUMMARY OF ARGUMENT

The Court of Appeals held that the underlying statute is "unconstitutional on its face," APP032 ¶ 15, but went on to say it could still bind the Petitioners because they signed a contract that incorporated the "rights, powers and duties as are prescribed by the [statute]." *Id.* ¶ 17. In other words, notwithstanding the fact that the law the contract purported to incorporate was unconstitutional, void, and

unenforceable, it could still be enforced because the Petitioners agreed to be bound by it.

This theory is untenable and dangerous. It is *untenable* because a facially unconstitutional statute is no statute at all, and thus by definition cannot be incorporated into a contract by operation of law. *Seaborn v. Wingfield*, 48 P.2d 881, 887 (Nev. 1935). Nor—except in equitable circumstances discussed in Section I.C below—can it be implemented by any branch of government. While private parties can, of course, form contracts to do things government itself cannot do, and can waive their constitutional rights, they cannot be *presumed* to do this; instead, such a waiver must be voluntary, knowing, and intelligent. *State v. Garcia-Contreras*, 191 Ariz. 144, 148 ¶ 14 (1998). Thus no waiver can be inferred or imposed by the boilerplate incorporation of law into a contract.

The contrary conclusion by the court below is *dangerous* because it would allow unconstitutional government actions to be insulated from judicial review—and enforced despite contradicting public policy—on the theory that private parties "agreed" to the terms of such statutes, even where that purported agreement is an inference based on ambiguous contractual recitations, as in this case. Allowing that would mean contracts that recite a requirement that citizens use their property or conduct their business consistently with then-existing statutes would be required—apparently forever—to (for example) allow their properties to be

searched or seized without lawful authority, or their speech or religion to be abridged, in ways that courts only later recognize as unconstitutional. That would amount not only to an *implied* waiver of constitutional rights, but a *mandatory* one. And it would make any legal determination of unconstitutionality into nothing more than a kind of time capsule: an unconstitutional law would still be enforced, perhaps decades later, because someone purportedly "agreed" to comply with it before a court declared it invalid. The principle of *lex loci contractus*, whereby "the municipal law of the State where the contract is so made, form[s] a part of it," *Ogden v. Saunders*, 25 U.S. (12 Wheat.) 213, 260 (1827), was never intended to become such an excuse for circumventing the Constitution.

ARGUMENT

I. An unconstitutional law is no law at all, and cannot be incorporated by contractual boilerplate.

A. A facially unconstitutional statute cannot be incorporated into a contract by operation of law.

As a general proposition, a contract implicitly incorporates the law in effect at the time and place of the contract's formation. *Foltz v. Noon*, 16 Ariz. 410, 414 (1915). But as Chief Justice Marshall recognized as long ago as *Ogden*, there must be limits to this *lex loci contractus* principle, because otherwise it would permit the legislature to entirely obliterate or unilaterally rewrite contractual obligations. 25 U.S. (12 Wheat.) at 337–38. Worse: if every statute, regardless of its

constitutionality, conscionability, or contrariness to public policy, is incorporated into a contract, then a subsequent judicial declaration that such statute is unenforceable would be essentially ineffective, because the ghost of that statute would remain in operation as a function of contract law—having been implicitly "agreed to" by all contracting parties.

That is not the law. On the contrary, an unconstitutional statute is a legal nullity, and cannot be incorporated by operation of law into a contract (although estoppel may sometimes require enforcement of such agreements as described in Section I.C below). That was the conclusion the Nevada Supreme Court reached in *Seaborn*, which involved an unconstitutional banking statute. That statute, adopted in 1911, made stockholders in banks individually liable to creditors in the event of a bank's insolvency. 48 P.2d at 882. The state Constitution, however, barred such liability. *Id.* Nevertheless, when the bank was declared insolvent in 1932, creditors sought to enforce the statutory liability, arguing that the stockholders had *contractually* waived the constitutional protection. *Id.* at 884. The court acknowledged that the laws in force at the time of a contract are typically incorporated into the contract—but held that statutes "in conflict with the Constitution, can in no wise form a part of such contract," and therefore that the stockholders could not be held to have implicitly waived constitutional safeguards by signing a contract. *Id.*

The *lex loci contractus* principle, said the court, only applies "'to the *valid* laws of the state. Only the provisions of the contract which are *legally enforceable* will control the parties thereto.'" *Id.* at 886 (emphases added; citation omitted). In fact, an unconstitutional law is "a dead limb on the legislative tree. An unconstitutional law is tantamount to no law at all. … '[I]t is, in legal contemplation, as inoperative as though it had never been passed.'" *Id.* at 887 (quoting *Norton v. Shelby County*, 118 U.S. 425, 442 (1886)).

One reason *Seaborn* emphasized this point is that holding otherwise would not only insulate unconstitutional laws from judicial review if "agreed to" by individual private parties, but would also govern cases in which *corporate charters*, which are a kind of contract, purport to incorporate statutes *in esse*.[1] The *Seaborn* court cited, for example, *Morse v. Metropolitan S.S. Co.*, 102 A. 524 (N.J. 1917), which involved an unconstitutional statute relating to receivership. There, the defendant corporation argued that the statute was unenforceable, to which the plaintiff replied that the corporation had "allowed itself to come into existence under a charter from the state, which was expressly subject to the liability that under conditions which come within the purview of the statute," and so "by

[1] Which corporate charters virtually always do. A sample Arizona corporate charter on the website eforms.com, for example, declares in Section 2, "The Corporation is organized under the relevant laws of the State of Formation ('Statutes'), and except as otherwise provided herein, the Statutes shall apply to the governance of the Corporation."

incorporating under the act," the company had "waived its rights." *Id.* at 526. The court rejected that proposition, holding that only *constitutional* laws are incorporated into a contract by operation of law. "The fact that the defendant incorporated under an act which contained an unconstitutional provision cannot render the provision enforceable, nor confer any power on the court to enforce it." *Id.*

This is not an exception to the *lex loci contractus* principle, but is inherent *in* that principle. That principle rests on the assumption that "the parties to the contract would have expressed that which the law implies 'had they not supposed that it was unnecessary to speak of it because the law provided for it.'" *Jack Spring, Inc. v. Little*, 280 N.E.2d 208, 215 (Ill. 1972) (citation omitted). But the highest law is the Constitution, not the statutes—and courts must therefore presume all the more that the parties would have expressed what the *Constitution* implies, had they not considered *that* unnecessary. After all, courts presume *against* the idea that parties intend to waive their constitutional rights, and require proof that such a waiver was voluntary, knowing, and intelligent. *Garcia-Contreras*, 191 Ariz. at 148 ¶ 14; *Webb v. State ex rel. Ariz. Bd. of Med. Exam'rs*, 202 Ariz. 555, 558 ¶ 10 (App. 2002). That means courts cannot presume that contracting parties meant to incorporate into their agreement statutes that

contradict the state's highest law, at least not without proof that such an intention was intelligent, knowing, and voluntary.[2]

Another reason an unconstitutional statute cannot form a part of a contract by mere operation of law is that this would render such contracts unenforceable on public policy grounds. "[A] court will not lend itself to the enforcement of an illegal contract … not because it endorses the conduct of either party but as a matter of public policy." *Brand v. Elledge*, 89 Ariz. 200, 204 (1961). A contract which purports to implement a facially unconstitutional law amounts to a contract to do an illegal thing. *See also Waggener v. Holt Chew Motor Co.*, 274 P.2d 968, 971 (Colo. 1954) ("Valid contracts may not arise out of transactions forbidden by law. The illegality inhering at the inception of such contracts taints them throughout and effectually bars enforcement.").

Of course, contracts alleged to violate public policy are not *per se* unenforceable in Arizona. *Zambrano v. M & RC II LLC*, 517 P.3d 1168, 1171 ¶ 1

[2] It might be argued that a statute is not unconstitutional until a court declares it so. But this is a positivist fallacy. (For one thing, it would mean that courts could never determine unconstitutionality, since every court would have to await a prior judicial determination of unconstitutionality before it could do so! *See* Green, *Legal Realism as Theory of Law*, 46 Wm. & Mary L. Rev. 1915, 1929 (2005) ("Since whatever a judge decides is law, there is simply no preexisting law to discover.")) As a logical matter, any facially unconstitutional statute has *always* been unconstitutional, even if courts only say so long after its enactment. To say otherwise is, among other things, to confuse the judicial and legislative roles, because it confuses a finding of unconstitutionality with repeal.

(Ariz. Sept. 28, 2022). Instead, courts balance the parties' interests with the public policy considerations at issue. *Id.* at 1173–74 ¶¶ 11–13. The court below, however, failed to consider such balancing, because it simply held that the contract's boilerplate purported to incorporate the laws then in effect, including unconstitutional ones. That was legal error which warrants reversal.

B. Private parties can contract to do things the Constitution does not authorize—but contractual boilerplate cannot keep an unconstitutional statute alive.

Private parties can, of course, agree to things that could not be legitimately imposed on them by statute. For example, a private club can discriminate based on classifications that the government may not consider, and members of a homeowners association can sign an agreement waiving their rights to display signs or symbols in their front yards, whereas imposing such a restriction on people by law would violate their freedom of speech. Likewise, if the members of a condominium association were to form a valid contract whereby each owner agreed that a bare majority's vote to sell would bind the dissenting minority, that contract would be valid, *cf.* *Stone v. Auslander*, 212 N.Y.S.2d 777, 780 (1961) (minority of corporate shareholders bound by majority); *Hodge v. U.S. Steel Corp.*, 54 A. 1 (N.J. App. 1903) (same), whereas for the legislature to impose such a rule would be—as the court below correctly held—an unconstitutional taking of private property for the benefit of private parties. APP032 ¶ 15.

But that is a different issue from the one presented here, which is whether the *lex loci contractus* rule can, via contractual boilerplate, enable a contracting party to exercise powers that originate not in agreement, but in an invalid statute. The answer is no, both because of the presumption against waiver of constitutional rights mentioned above, and because the source of the authority in question is different in the two situations. Where parties *agree* to empower an entity to do certain things—such as allowing a corporate majority to bind a minority—they are vesting it with their own *innate* authority over their own liberty and property. The source of that power is *consent*: the minority is choosing to exercise their own rights in a certain way (i.e., to surrender to the majority). But here, the power in question derives (or would, if the statute were constitutional) *not* from consent, but from the (unconstitutional) statute. If the statute were constitutional, the power being exercised would obviously be a delegated police power, *not* a power rooted in consent. But because the statute is *un*constitutional, the Condominium Association cannot lay claim to that delegated police power. It can therefore only require the minority property owners to acquiesce if it can trace that power to some consensual agreement. It cannot do that here, because its sole source of purported power is the contractual recitation that it can exercise "rights, powers and duties as are prescribed by the [statute]," *id.* ¶ 17, and that language cannot transform the

nature of the power from one (purporting to be) derived from the police power into one derived from consent.

C. Equitable considerations can sometimes require enforcement of invalid contracts, but no such considerations have been shown here.

Reliance interests and other equitable considerations can sometimes require parties to comply with agreements that have subsequently been found to be contrary to law. Just as contracts against public policy can sometimes still be enforced, *Zambrano*, 517 P.3d at 1173–74 ¶¶ 11–13, so parties who enter into contracts as a consequence of statutes later held unconstitutional can still be bound by those contracts. *See, e.g.*, *Coltec Indus., Inc. v. Hobgood*, 280 F.3d 262, 271–77 (3d Cir. 2002); *Brady v. United States*, 397 U.S. 742, 757 (1970). That is why, e.g., someone who settles a lawsuit is not entitled to later be relieved of the settlement on the grounds of a subsequent change in controlling law. *See, e.g.*, *Ehrheart v. Verizon Wireless*, 609 F.3d 590 (3d Cir. 2010).[3] Likewise, a party that

[3] *Ehrheart* explained that "a litigant's decision to settle …, when voluntarily made, [are] *calculated and deliberate* choices … . [T]he decision to settle a case is a *considered* one … [which] implicitly acknowledges calculated risks and, in the end, reflects the *deliberate decision* of both parties to opt for certainty in terminating their litigation." *Id.* at 595–96 (emphases added). But in a case like this, there was no calculated and deliberate decision to opt out of the constitutional protections at issue. On the contrary, the parties agreed to be bound by the law—and the statute was not the law, because it was facially unconstitutional. Thus the equitable considerations which have led courts in cases like *Ehrheart* to continue enforcement of a contract that has become contrary to law are not present here.

receives benefits from an agreement may sometimes be estopped from denying the validity of that agreement, even if it turns out to be legally invalid. *See*, *e.g.*, *Bldg. & Loan Ass'n of Dakota v. Chamberlain*, 56 N.W. 897, 900 (S.D. 1893); *Perkinson v. Hoolan*, 81 S.W. 407, 407–08 (Mo. 1904).

But such estoppel is grounded on factors such as reliance. *See* *Cumberland Cap. Corp. v. Patty*, 556 S.W.2d 516, 540–41 (Tenn. 1977) (explaining in detail why contracts premised on unconstitutional laws are voidable, but not necessarily void). *Cf.* *Jones v. Preuit & Mauldin*, 851 F.2d 1321, 1323–28 (11th Cir. 1988) (private parties entitled to qualified immunity for acting in good faith in reliance on statute later declared unconstitutional); *DeVargas v. Mason & Hanger-Silas Mason Co.*, 844 F.2d 714, 724–25 (10th Cir. 1988) (same). Because these are *equitable* considerations, they do not disturb the *legal* point made above, that an unconstitutional statute cannot be given life by being incorporated into a contract by operation of law.

But equitable considerations require inquiry into reliance, hardships, and clean hands—and the court below never discussed or weighed these or any other equitable considerations, because it never addressed the question of estoppel. If circumstances exist that would entitle the Respondents to estop the Petitioners from denying the validity of the power to compel them to sell their property, both sides should be given a chance to brief those equitable questions on remand.

II. The theory adopted below is dangerous to constitutional rights.

Not only is the decision below illogical and contrary to law, but it establishes a dangerous precedent that effectively insulates unconstitutional statutes from judicial control. Under that decision, the ghosts of laws declared unenforceable would continue to haunt contracting parties into the indefinite future—perhaps forever. A contract or corporate charter which purports to incorporate all laws *in esse* might remain in effect for decades, long after the underlying laws are declared invalid.

Consider: if this case involved a statute that, for example, prohibited the sale of real property to members of a racial minority—such as California's Alien Land Law[4]—no court would imagine that such an unconstitutional statute could be implicitly incorporated into a contract—and that contracting parties could continue to effectuate its mandates—due to boilerplate language saying that all laws *in esse* at the time of contract formation are incorporated therein. *Cf.* *Kaneda v. Kaneda*, 45 Cal. Rptr. 437, 444 (Cal. App. 1965) ("If the Alien Land Act is as inoperative as though it had never been passed, plaintiff cannot now rely upon it.").

Yet recent years have seen federal courts increasingly indulging the theory that contracts can keep unconstitutional government actions alive. This is most

[4] Adopted in 1913, the Law forbade the sale of land to Asians. It was not declared unconstitutional until 1952. *See Sei Fujii v. State*, 38 Cal.2d 718 (1952).

noticeable in the realm of public employee constitutional rights in the wake of *Janus*, 138 S. Ct. 2448. That case held it unconstitutional for public sector unions to force non-members to pay agency fees to the unions. Since then, plaintiffs have sought to enforce these rights, only to find lower courts declaring that because they joined a union prior to the *Janus* decision, they waived their constitutional rights.

Thus, for example, in *Savas v. Cal. State L. Enf't Agency*, 485 F. Supp. 3d 1233 (S.D. Cal. 2020), *aff'd*, 2022 WL 1262014 (9th Cir. Apr. 28, 2022), a group of lifeguards who joined the union before *Janus* was decided sought afterwards to resign from the union—only to be told they could not, because the union formed a collective bargaining agreement forbidding members from resigning for four years. The court ruled against them because the membership agreement said "there are limitations on the time period for [resigning]," *id.* at 1235, which the Court of Appeals said bound them as a contractual matter even though the four year non-resignation rule was adopted only *after* they signed the agreement.[5]

Likewise, in *Fisk v. Inslee*, 759 Fed. Appx. 632 (9th Cir. 2019), people who joined unions prior to *Janus*—and whose membership cards said the union would deduct dues for a minimum of one year, and that members could only opt out of paying dues during one annual two-week window, resigned within the first year. *Id.* at 664. When they sued to recoup the money the union had taken from them,

[5] A petition for certiorari is now pending in this case.

the Ninth Circuit held—despite the *Janus* decision's clear statement that it is unconstitutional for public sector unions to take money from workers without their prior, clear, and affirmative consent—that they could not sue because they had signed the membership agreements and had therefore consented to the taking of their money. *Id.*

Such illogical outcomes illustrate the problem with a rule whereby unconstitutional laws can be shielded from judicial action on a *lex loci contractus* theory. That cannot be the right outcome—and that warrants reversal.

CONCLUSION

The petition should be *granted*.

Respectfully submitted this 18th day of November 2022 by:

/s/ *Timothy Sandefur*
Timothy Sandefur (033670)
Scharf-Norton Center for Constitutional Litigation at the
GOLDWATER INSTITUTE