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Rent Waivers, a Pandemic and the Contracts Clause

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By **Andrew J. Luskin** | May 07, 2020

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As the current COVID-19 pandemic continues its path of destruction, the New York State Senate and Assembly are considering identical bills (Senate Bill S8125A; Assembly Bill A10224A) to ease residential and small business rent burdens in this time of economic hardship. The proposed legislation would waive rent payments for residential tenants and small businesses that have suffered the loss of income or have been forced to close their place of business as a result of government ordered pandemic-related restrictions. While the intention of helping those in need is admirable, the proposed legislation would alter private contract rights, and therefore inescapably bump up against the Contracts Clause of the U.S. Constitution.

The pending bills would not provide a mere rent-payment delay for those entitled to the benefit, with missed payments to be made up later. Rather, by the very text of the proposed legislation, those entitled to benefit from a 90-day rent waiver "shall not and shall never be required to pay any rent waived during such time period." The bills, however, provide no yardstick as to how much lost income would be necessary to trigger the rent waiver. Would *any* amount of lost income entitle a tenant to the rent waiver? Would this apply to individuals who are self-employed and claim a loss of self-employment income? And what about a tenant who has sufficient unearned (i.e., investment) income but lost his or her job to COVID-19? The proposed legislation leaves these and other important questions unanswered.

In aid of landlords, the bills also provide that "[a]ny person who faces a financial hardship as a result of being deprived rent payments for a covered property pursuant to this section shall receive forgiveness on any mortgage payments for such covered property." The proposal provides a method to determine the amount of mortgage forgiveness based on a formula that considers the percentage of total rent that a landlord loses on a property as compared to the total rent roll on the property. Each of the Senate and Assembly bills has been referred to its respective house committee. On April 22, 2020, the New York City Council referred to council committee a proposed resolution calling on the New York Legislature to enact the proposed Senate and Assembly bills.

The Contracts Clause

Unconstitutional legislation, however well intentioned, is still unconstitutional. The proposed rent-waiving legislation bristles with constitutional repugnancy. Article 1, Section 10, Clause 1 of the United States Constitution provides that "[n]o State shall … pass any … Law impairing the Obligation of Contracts." Yet the New York Legislature, which possibly might be urged by the New York City Council, is considering doing just that.

The Contracts Clause was a reaction to legislation enacted after the Revolutionary War that was designed to repudiate or adjust pre-existing debtor-creditor relationships after a tumultuous period that strained debtors' abilities to repay their obligations. See *Keystone Bituminous Coal Ass'n v. DeBenedictis,* 480 U.S. 470, 502-03 (1987). "The widespread distress following the revolutionary period and the plight of debtors had called forth in the States an ignoble array of legislative schemes for the defeat of creditors and the invasion of contractual obligations." *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398, 427 (1934). Writing under the pseudonym "Publius" in The Federalist No. 44, James Madison lobbied for a constitutional restraint on such state curtailment of private contract rights. The Contracts Clause has had a tortuous and somewhat confusing history in the high court. Depression-era cases provided substantial leeway to states to use their police powers to stem the biting economic effects of the Great Depression.

'Blaisdell' and 'Worthen'

In *Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. 398 (1934), the court upheld Minnesota's statutory moratorium on home foreclosures as an emergency measure permitted by the state's police power in the midst of the Great Depression. The statute did not impair the integrity of mortgage indebtedness, but only the ability of the mortgagee to enforce its rights by operation of an extended redemption period for the mortgagor. The Supreme Court upheld the moratorium because it was addressed to a "legitimate end and the measures taken [were] reasonable and appropriate to that end." Id. at 438.

A few months after *Blaisdell*, the Supreme Court decided *W.B. Worthen Co. v. Thomas,* 292 U.S. 426 (1934), this time invalidating state legislation as violative of the Contracts Clause. Justice Hughes, who wrote the *Blaisdell* decision over the dissent of four other justices, now sided with Justice Sutherland, the chief dissenting voice in *Blaisdell*. The plaintiff Worthen recovered a money judgment against the Thomases for their non-payment of rent. Worthen then garnished a life insurance company that was indebted to Mrs. Thomas, then a judgment debtor, for life insurance proceeds after her husband passed away. The garnishment became a lien prior to enactment by the Arkansas Legislature of a law exempting life insurance proceeds from judgment attachment. Mrs. Thomas thereupon moved to dismiss the garnishment. Worthen countered that the new law violated the Contracts Clause. The court agreed, while distinguishing *Blaisdell* as an example of state action providing "temporary and conditional" relief that was "reasonable, from the standpoint of both mortgagor and mortgagee," and "limited to the exigency to which the legislation was addressed." *Worthen*, 292 U.S. at 434. In contrast, observed the court, the Arkansas law involved state remedial action ostensibly intended to address an emergency, but was "neither temporary nor conditional," and instead "plac[ed] insurance moneys beyond the reach of existing creditors," as an emergency measure, without "limitations as to time, amount, circumstances, or need." Id.

The Supreme Court considered a number of other Contracts Clause cases in the ensuing years, striking down state laws in five of twenty such cases from 1934 through 1937. See David F. Forte, *Forgotten Cases: Worthen v. Thomas,* 66 Clev. St. L. Rev 705, 713 (2018). Supreme Court sentiment for a time after the depression years seemed to tip the scales of Contracts Clause jurisprudence back in favor of the *Blaisdell* approach. See Forte, 66 Clev. L. Rev. at 720 ("The post-New Deal Court decided that it was inappropriate for a judicial body to second-guess economic decisions by legislative bodies, whether state legislatures or Congress"). *Blaisdell*, *Worthen*, and later cases eventually gave rise to a new test that looked to "whether a state law has, in fact, operated as a substantial impairment of a contractual relationship." *Allied Structural Steel v. Spannaus*, 438 U.S. 234, 243 (1978). If so, then the consideration turns to whether the legislation was "necessary to meet an important general social problem." Id. at 247. Notably, since *Allied Structural Steel*, the Supreme Court has not voided any state law under the Contracts Clause. *See* Forte, 66 Clev. L. Rev. at 722.

'Sveen v. Melin'

The Supreme Court last considered the Contracts Clause in *Sveen v. Melin*, 138 S. Ct. 1815 (2018). A 2002 Minnesota law provided that the dissolution or annulment of a marriage automatically revoked a revocable life insurance beneficiary designation made by a spouse in favor of the other spouse prior to divorce. The court observed that the legal system "has long used default rules to resolve estate litigation in a way that conforms to decedents' presumed intent." Id. at 1819. Under prior Minnesota law, divorce did not affect a beneficiary designation, although a particular divorce decree could do so. Sveen and Melin married in 1997. The following year, Sveen purchased a life insurance policy naming Melin as the primary beneficiary and his two children from a prior marriage as contingent beneficiaries. Sveen and Melin divorced in 2007. The divorce decree made no mention of the insurance policy, and Sveen took no action to revise his beneficiary

designations before he passed away in 2011. Melin and the Sveen children made competing claims to the policy proceeds. Under the Minnesota revocation-on-divorce law, the children would win. But Melin argued that the law violated the Contracts Clause as an impermissible impairment of a contract.

The federal district court sided with the children, the U.S. Court of Appeals for the Eighth Circuit reversed, and the Supreme Court reversed the circuit court, holding that "three aspects of Minnesota's law, taken together, defeat Melin's argument" that the revocation-on-divorce law "'severely impaired'" her ex-husband's contract. Id. at 1822 (quoting Melin's brief). First, held the court, the statute is "designed to reflect a policyholder's intent – and so to support, rather than impair, the contractual scheme." Id. Second, "the law is unlikely to disturb any policyholder's expectations because it does no more than a divorce court could always have done." Id. Third, "the statute supplies a mere default rule, which the policyholder can undo in a moment." Id. The Minnesota law thus "stacks up well," id., against other state laws that the court has upheld. The court concluded that the revocation-on-divorce scheme actually "often honors, not undermines, the intent of the only contracting party to care about the beneficiary term," id. at 1823, and therefore does not impair the contract in violation of the Contracts Clause.

As the most recent Contracts Clause pronouncement of the Supreme Court, *Sveen* may be highly suggestive that the proposed legislative rent waiver for the private sector would *not* pass Contracts Clause scrutiny. The proposed bills would purport to waive—not delay—private contract obligations with no recourse, remedy, or redress for landlords. In contrast, the present moratorium on evictions in New York delays an extra-contractual remedy without actually altering private contract obligations. That the proposed legislation also would provide some offsetting benefit for landlords with mortgage obligations would do nothing for those landlords without the encumbrance of a mortgage. And with or without a mortgage, landlords use rental income to fund other incidences of property ownership, as well as personal expenses. The proposed rent waiver thus stands in stark contrast to the circumstances in *Sveen* upon which the Supreme Court relied to validate Minnesota's revocation-on-divorce statute. Here, the rent waivers would not further an interest of landlords or provide a mere default scheme from which landlords could opt out.

A Proposed Solution for Landlords and Tenants

Instead of pursuing legislation that appears to violate the Contracts Clause, the Legislature might consider carefully-crafted, temporary revisions to Real Property Actions and Proceedings Law (RPAPL) Article 7, which governs summary eviction proceedings in New York. By way of example, the non-payment summary proceeding process could be re-tooled expressly to afford judges flexibility in dispensing the statutory remedy of eviction on a case-by-case basis according to criteria that fairly account for the needs, rights, and interests of both landlord and tenant during the COVID-19 exigency. The parties' respective abilities to withstand the financial hardships of the pandemic could be explored at an initial case conference, where both sides are permitted to present documentary proof (i.e., disclosures of earned and unearned income; proof of mortgage, taxes, and building maintenance expenses; and the like) relevant to a set of defined criteria that ultimately could dictate the availability and timing of the remedy of eviction. The loss of employment due to COVID-19 might put a paycheck-to-paycheck tenant in dire straits, but not deprive another tenant who lost employment to the pandemic of the ability to pay rent from other income sources. A landlord with few tenants might document an urgent need timely to receive rent to pay a mortgage, taxes, insurance, and other upkeep, or to satisfy personal or other household expenses. A landlord with more tenants, in contrast, might have the resources to

sustain itself for a longer period with receipts from rent-payment tenants. In sum, temporary legislation establishing criteria that address the rights, interests, and financial wherewithal of both landlord and tenant when fashioning a judgment could ameliorate the COVID-19 emergency more judiciously and without running roughshod over constitutional rights.

Conclusion

The Legislature should suspend any further consideration of S8125A and S10224A. Although well intentioned, the proposed legislation is overbroad, presents serious constitutional issues, and would work a manifest and unnecessary injustice on landlords. The Legislature instead should consider temporary revisions to RPAPL Article 7 to fairly balance the rights and capabilities of both landlord and tenant as they may be affected by the current pandemic. In steering away from a Contracts Clause violation, the Legislature also should be properly counseled to ensure that that any such temporary statutory amendments do not go so far as to violate due process rights.

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