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Executive Order on Residential Security Deposits: Constitutional Concerns Intersect With Emergency Powers

A New Jersey court is likely to find that allowing tenants to access their security deposits is rationally related to the promotion of a safe and stable housing environment during a public health emergency.

By **Kevin W. Weber** | May 06, 2020 at 10:30 AM

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Since the outbreak of the coronavirus, Gov. Murphy has issued more than two dozen executive orders. Most recently, Executive Order No. 128 (E.O. 128) issued on April 24, 2020, provided relief for residential tenants by allowing the tenant to direct his or her landlord to apply the tenant's security deposit to rent payments that become due and owing after the "State of Emergency" declaration on March 9, 2020.

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More than 850,000 New Jersey residents filed unemployment claims since mid-March, likely resulting in many missed rent payments. There is no question that Gov. Murphy's order will help New Jersey residential tenants stay out of default and make their April and May rent payments. Many view this as a rational policy decision. In addition to providing stable housing for tenants, there are other potential benefits. Millions of dollars in residential security deposits sit untapped in bank accounts. The governor's executive order provides much-needed liquidity to the residential real estate economy—landlords will receive millions of dollars in rent payments that likely would have gone unpaid, thereby helping landlords pay their own mortgages and stay out of default (and even foreclosure) with their lenders. But, putting aside the rationality of the policy and its likely societal benefit, particularly to hard-hit tenants, was it constitutional and within the scope of his emergency powers?

E.O. 128 Likely Does Not Violate the Contracts Clause

Within days of the announcement of E.O. 128, questions were raised by legislators and others as to whether this order violates the Contracts Clause of the New Jersey Constitution, as it is a law "impairing the obligation of contracts." More than likely, E.O. 128 would survive a challenge under this legal theory.

The Supreme Court of New Jersey has summarized, that "[b]oth the New Jersey and Federal Constitutions prohibit the passage of laws impairing the obligation of contracts." *Burgos v. State*, 222 N.J. 175, 193 (2015) (citing U.S. Const. art. I, § 10, cl. 1 ("No State shall … pass any … Law impairing the Obligation of Contracts …."); N.J. Const. art. IV, § 7, ¶ 3 ("The Legislature shall not pass any … law impairing the obligation of contracts, or depriving a party of any remedy for enforcing a contract which existed when the contract was made."). The test for a contract impairment claim "first examines whether a change in state law results in the substantial impairment of a contractual relationship and, if so, then reviews whether the impairment nevertheless is 'reasonable and necessary to serve an important public purpose.'" *Berg v. Christie*, 225 N.J. 245, 259 (2016) (quoting *U.S. Tr. Co. of N.Y. v. New Jersey*, 431 U.S. 1, 25 (1977).

Unquestionably, E.O. 128 impairs thousands of private contracts (leases), as it upends the negotiated obligations in the security deposit clause of virtually every residential lease. But, this impairment alone does not carry the day, as it ignores the critical second portion of the test. "Not even a substantial impairment of contract violates the constitution if the governmental action has a 'significant and legitimate public purpose,' is based upon reasonable conditions, and is related to 'appropriate governmental objectives.'" *Borough of Seaside Park v. Comm'r of N.J. Dep't of Educ.*, 432 N.J. Super. 167, 216 (App. Div. 2013) (quoting *State Farm Mut. Auto Ins. Co. v. State*, 124 N.J. 32, 64 (1991). In the current state of emergency, it is hard to imagine a court striking down E.O. 128, as doing so would require a finding that the objectives were not reasonable under the conditions. In this crisis, Gov. Murphy's order more would likely survive a Contracts Clause challenge.

E.O. 128 May Usurp Legislative Regulation of Security Deposits

There is, however, a more nuanced question as to whether E.O. 128 is Constitutional—separation of powers principles. Under long-standing New Jersey precedent, "[e]xecutive orders, when issued within their appropriate constitutional scope, are an accepted tool of gubernatorial action." *Commc'ns Workers of Am., AFL-CIO v. Christie*, 413 N.J. Super. 229, 254 (App. Div. 2010). The scope of that authority, however, depends on various circumstances. For example, where one branch has delegated authority to another, or deliberately chose to share its own power with another branch, the delegation or sharing will likely be upheld. *Id.* at 257. But, alternatively, an executive action is less likely to be upheld where the action "impairs the essential integrity" of another branch, such as the legislature. *Id.* (quoting *Massett Bldg. Co. v. Bennett*, 4 N.J. 53, 57 (1950)). Thus, "[a]n executive order is invalid if it usurps legislative authority by acting contrary to the express or implied will of the Legislature." *Id.* at 259. "Simply put, an Executive Order cannot amend or repeal a statute." *Williamson v. Treasurer*, 357 N.J. Super. 253, 272 (App. Div.), *certif. denied*, 177 N.J. 493 (2003). Thus, courts have nullified gubernatorial executive orders where they create new exemptions not found in the statute (*Williamson*), or change or expand the meaning of statutorily defined terms (*CWA v. Christie*).

The legislature has long regulated residential security deposits. *See* N.J.S.A. 46:8-19 (enacted 1967). The legislature requires that:

- Deposits are limited to an amount equal to 1 ½ months rent, N.J.S.A. 46:8-21.2;
- Security deposits be deposited in an interest bearing account, N.J.S.A. 46:8-19(a)(1);
- The account must be at a New Jersey or federal chartered bank, N.J.S.A. 46:8-19(a)-(b);
- The landlord must give the tenant written notice of where the money is deposited, N.J.S.A. 46:8-19(c);
- The landlord must give the tenant notice if the account is moved, and provide annual notices of the interest earned, N.J.S.A. 46:8-19(c);
- The deposit must be returned within 30 days of the termination of the tenancy, N.J.S.A. 46:8-21.1;
- The deposit must be returned within five days in the case of a tenant displaced by fire, flood, evacuation, or by a building code official prohibiting occupancy, N.J.S.A. 46:8-21.1;
- None of the above regulations are waivable under the lease, N.J.S.A. 46:8-24.

If a landlord improperly withholds a security deposit, he may be "liable for a civil penalty of not less than $500 or more than $2,000 for each offense," and may face an action by the tenant where the court must award "double" the amount of the deposit and may award attorney fees. N.J.S.A. 46:8-21.1. All told, [t]his legislation was intended to protect tenants from overreaching landlords who seek to defraud tenants by diverting rent security deposits to their own use." *Jaremback v. Butler Ridge Apartments*, 166 N.J. Super. 84, 87 (App. Div. 1979).

By any measure, the legislature is heavily invested in the regulation of residential security deposits. But, one way in which the legislature purposefully did *not* regulate security deposits was to direct the conditions on which the landlord could access the deposit, other than to say that "no deductions shall be made from a security deposit of a tenant who remains in possession of the rental premises." N.J.S.A. 46:8-21.1. (In other words, if there is damage to the premises, the landlord cannot tap the security

deposit until after the tenant vacates; likewise if there is a non-payment of one month rent, the landlord cannot utilize the deposit unless the tenant is evicted). Rather, the legislature allowed for the landlord and tenant to contractually agree on the allowable uses of the security deposit, as the statute states that the deposit shall be for "the use in accordance with the terms of the contract, lease or agreement." N.J.S.A. 46:8-19. Thus, there is no suggestion in the statute that the legislature desired to force landlords to use the security deposit in such non-payment situations —in fact, the opposite is likely true, as there is a clear legislative intent to not allow the use of the deposit during the tenancy.

What is more, there is no fair reading of the statute that suggests the legislature intended to cede its regulation of this area to the executive branch. It is, of course, a closer call as to whether E.O. 128 *conflicts* with the security deposition legislation. Arguably, by directing that the use of the security deposit should be governed by contract, the legislature made an express choice not to list specific allowable uses for those funds. Sometimes, a legislative omission is "conspicuous and instructive." *CWA*, 413 N.J. Super. at 271. Where the "desired changes in the law would, in essence, require not only a pen, but also an eraser," *id.*, it can be surmised that the executive order runs afoul of the statute. (And here, Gov. Murphy may have understood there to be some inconsistency between his order and the current law, as E.O. 128 says "[a]ny provisions of N.J.S.A. 46:8-19 et seq. that are not inconsistent with this Order remain in full force and effect.") A challenge to E.O. 128 on this basis is plausible, but will likely be balanced against the unique emergency in which the state finds itself today, as explained below.

Emergency Powers and E.O. 128

The preamble of E.O. 128 cites various statutes conferring emergency powers on the governor. However, it is not clear that any of these emergency powers allows the governor to take the actions related to security deposits in E.O. 128. The broadest powers are in the Disaster Control Act, N.J.S.A. App. A:9-33, seq. ("DCA"). Under the DCA, the governor may "commandeer and utilize ... any privately owned property necessary to avoid or protect against any emergency subject to the future payment of the reasonable value of such services and privately owned property as hereinafter in this act provided." N.J.S.A. App. A:9-34. *See also* N.J.S.A. App. A:9-51 (allowing governor to temporarily employ "real or personal property" for purposes "promoting the public health, safety or welfare.")

But, it does not appear that E.O. 128 is issued pursuant to this commandeering power, as there is no mention in E.O. 128 of any future repayment of the security deposits, and the use of the deposits is not "temporary," insofar as E.O. 128 does not require the deposits to be repaid (unless the lease is later renewed). The DCA also contains a broad provision stating that "the Governor is empowered to make such orders, rules and regulations as may be necessary adequately to meet the various problems presented by any emergency," N.J.S.A. App. A:9-45, including "[o]n any matter that may be necessary to protect the health, safety and welfare of the people or that will aid in the prevention of loss to and destruction of property." N.J.S.A. App. A:9-51(i). While E.O. 128 does not fit perfectly into this provision, broadly speaking, the purpose of the order is to protect the health, safety, and welfare of tenants by ensuring they will have a stable residence for the duration of the crisis. Under emergency powers precedent, this may be enough.

The Supreme Court of New Jersey has stated that, "in reviewing executive actions undertaken pursuant to delegated emergency powers, we must determine whether the actions are authorized by the statute." *Worthington v. Fauver*, 88 N.J. 183, 197-98 (1982). That analysis is a two-part test, "first, a determination of whether the Executive Order bears a rational relationship to the legislative goal of protecting the

public. Second, the executive action must be closely tailored to the scope of the current emergency situation." *Id.* In the *Worthington* case, the court was reviewing Gov. Byrne's executive order declaring an emergency regarding prison overcrowding and directing county correctional facilities to house state prisoners. While the plain language of the DCA may not have squarely supported Gov. Byrne's exercise of his emergency powers for prison overcrowding, the court took a broad reading of a statute designed to "protect the public health, safety and welfare," and affirmed the governor's remedial actions to address the situation.

As noted at the outset, New Jersey may soon face over a million additional unemployed residents, and the maintenance of secure and safe housing is, without question, within the public interest. Thus, even if the DCA does not squarely address the governor's ability to address a housing situation, a New Jersey court is likely to find that allowing tenants to access their security deposits is rationally related to the promotion of a safe and stable housing environment during a public health emergency.

Conclusion

E.O. 128 may very well violate separation of powers principles, in that it interferes with and upends a very deliberative statutory scheme. It may also have unintended and unforeseen consequences—how will property damage at the end of the lease term be addressed? What incentive will most tenants have to pay the final month of rent? However, in light of the public health emergency, the governor's broad powers conferred by the legislature will make it difficult to challenge this policy as unconstitutional.

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