No. 21-1795

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

MATTHEW JOHNSON, *et al.*,
Appellants,
v.

GOVERNOR OF NEW JERSEY, *et al.*,
Appellees.

On Appeal from the United States District Court for the District of New Jersey
No. 1:20-cv-06750, the Honorable Noel L. Hillman

APPELLANTS' OPENING BRIEF & APPENDIX VOL. 1 (pp. 1-44)

NEW CIVIL LIBERTIES ALLIANCE
JARED MCCLAIN
MARK CHENOWETH
RICHARD A. SAMP
HARRIET HAGEMAN
KARA ROLLINS
1225 19th St. NW, Suite 450
Washington, DC 20036
(202) 869-5210
Jared.McClain@NCLA.legal
Counsel for Appellants

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JURISDICTIONAL STATEMENT

Pursuant to 28 U.S.C. § 1291, this Court has jurisdiction to review the final decision of the United States District Court for the District of New Jersey, which dismissed Appellants' claims in their entirety pursuant to Rule 12(b)(6).

RELATED CASES & PROCEEDINGS

Appellants are not aware of any related case or proceeding before this Court or any other federal court. Appellants have a separate case in the Appellate Division of the Superior Court of New Jersey, raising distinct challenges to Executive Order 128 under state law. *See Kravitz, et al. v. Murphy, et al.*, No. A-1584-20 (argued June 1, 2021). The outcome of the state-court action does not bear on the federal issues in this appeal.

ISSUES PRESENTED

Appellants present the following issues for this Court's review:

I. Whether the trial court erred in granting substantial deference to Governor Murphy's unilateral judgment.

II. Whether the trial court erred in ruling that Appellants did not state a claim under the Contracts Clause of the United States Constitution.

STANDARD OF REVIEW

This Court "review[s] de novo a district court's grant of a motion to dismiss for failure to state a claim under Federal Rule of Civil Procedure 12(b)(6)." *United States v. One (1) Palmetto State Armory PA-15 Machinegun Receiver/Frame*, 822 F.3d 136, 140 (3d Cir. 2016). In doing so, this Court must "accept as true all allegations in the complaint and all reasonable inferences that can be drawn from them after construing them in the light most favorable to the nonmovant." *Id.* (citation omitted).

SUMMARY OF ARGUMENT

The Founders included the Contracts Clause in the United States Constitution to prevent states from relieving a favored constituency of its contractual obligations. No strangers to national emergency, the Founders knew from living under the Articles of Confederation that state interference with contractual rights destroyed trust in contracts and damaged the national economy. The Contracts Clause restored the public's faith in private contracts, allowing the nation's economy to grow into the world's largest.

By committing two significant errors of law, the trial court effectively wrote the Contracts Clause out of the Constitution. In the trial court's view, once a state regulates an industry, contracting parties within that industry may no longer have any expectation that their contractual rights will be free from governmental—or mere gubernatorial—nullification. And, according to the trial court, federal courts *must* give substantial deference to a state's—or governor's—decision to impair private contractual rights. These legal errors render useless the Contracts Clause itself and innumerable private contracts that depend on that clause for protection.

The Supreme Court has reiterated that the Contracts Clause "remains part of the Constitution. It is not a dead letter." *Allied Structural Steel Co. v. Spannaus*, 438 U.S. 234, 241 (1978). So, the clause "must be understood to impose *some* limits upon the power of a State to abridge existing contractual relationships, even in the exercise of its otherwise legitimate police power." *Id.* at 242. The trial court ignored those limits, and

its decision threatens to return contractual rights to the precarity they suffered under the Articles of Confederation. Appellants ask this Court to vindicate the Contracts Clause and restore the federal judiciary to its proper constitutional role.

BACKGROUND

Governor Philip D. Murphy has estimated that, in New Jersey, "[t]here are thousands, maybe hundreds of thousands, if not millions of contracts between landlords and renters." *See* NJ.com, *Corona Virus in New Jersey: Update April 11, 2020*, YouTube, at 47:54, *available at* https://bit.ly/3pvPZvH. For over a century, these contracts have commonly required New Jersey tenants to pay a security deposit as an express condition of the lease. *See, e.g.*, *Hecklau v. Hauser*, 59 A. 18, 18 (N.J. Sup. Ct. 1904). Housing providers can negotiate a deposit of up to one-and-a-half months' rent, or about 12.5% of the contract's annual value. *See* N.J.S.A. 46:8-21.2. The deposit insures the property against damage that may occur during the tenancy, thereby mitigating the housing provider's risk of losing their entire profit from the transaction (and then some) and incentivizing the tenant to leave the unit in good repair. To maintain that security, Appellants, like many housing providers, negotiated a provision in their leases that prohibited their tenants from using the security deposit to pay rent without the Appellants' permission. (App.141, 161, 175).

These express terms governed the contracting parties' incentives and behavior during residential tenancies in New Jersey up until April 24, 2020, at which point

Governor Murphy unilaterally nullified those contractual rights and obligations, as he altered the parties' contractual terms in a lopsided manner to which no housing provider would have agreed in an arm's-length negotiation.

A. Appellants Are Small-Scale Housing Providers

Appellants Margarita and John Johnson are residents of Vineland, New Jersey. They own and operate Appellant Two Bears Property Management and are co-trustees of the Johnson Trust, which owns a residential duplex in Vineland (the "Sixth Street Property"). (App.152). The Johnsons rent the property pursuant to a written lease (the "Sixth Street Lease") executed on July 31, 2017. (App.161). Under the lease, the tenant agreed to lease the Sixth Street Property from August 1, 2017, through July 31, 2019, for $820 per month. (App.161). The Johnsons and the Sixth Street Tenant continue to operate under the terms of the Sixth Street Lease on a month-to-month tenancy.

The lease required the Sixth Street Tenant to pay a security deposit of $1,230 on the execution of the lease. (App.161). The Sixth Street Lease also set out the terms governing the parties' rights and obligations with respect to the security deposit due under the lease:

> **SECURITY DEPOSIT.** On execution of this lease, Lessee deposits with Lessor One Thousand Two Hundred Thirty Dollars ($1230.00), the sum equal to one and one-half (1.5) months' rent, receipt of which is acknowledged by Lessor, as security for the faithful performance by Lessee of the terms hereof, to be returned to Lessee, with interest except where required by law, on the full and faithful performance by them of the provisions hereof.

(App.161). The lease allowed the Johnsons to deduct from the security deposit "[t]he cost of all damages; to include materials, labor and any applicable taxes." (App.161).

Appellants Charles Kravitz and Dawn Johanson-Kravitz are residents of Mullica Hill, New Jersey. They own and operate Appellant Little Harry's LLC, which leases a residential property that the Kravitzes own in Glassboro, near Rowan University (the "Glassboro Property"). (App.137). On August 3, 2019, the Kravitzes rented the Glassboro Property to four Rowan students (the "Rowan Tenants") pursuant to a residential lease agreement (the "Glassboro Lease"). (App.139). The Rowan Tenants agreed to lease the Glassboro Property from August 15, 2019, through June 1, 2020, for $2,000 per month in rent. (App.140).

The Rowan Tenants also agreed to pay a security deposit of $2,000, which the Kravitzes would "hold … in an interest bearing account." (App.141). The Glassboro Lease specified that the Kravitzes could "make deductions from the Security Deposit" to cover ten enumerated costs, and it expressly forbade the Rowan Tenants from "us[ing] the Security Deposit as payment for Rent." (App.141-42). Under the terms of the lease, the Kravitzes would return the Security Deposit "less any proper deductions" "[w]ithin the time period required by law and after termination" of the lease. (App.142).

Appellant Andrew Van Hook is a resident of Millville, New Jersey. He is the managing member of Appellant Union Lake Enterprises, LLC, which owns a residential property in Millville (the "Millville Property"). (App.169). Union Lake Enterprises rents

the property to the "Millville Tenant" pursuant to a "New Jersey Realtors® Standard Form of Residential Lease" agreement (the "Millville Lease"), which the parties executed on June 26, 2018. (App.174).

The Millville Tenant initially agreed to lease the Millville Property for $1,450 per month, from August 1, 2018, through June 30, 2020. (App.175). On June 22, 2020, the parties executed an addendum extending the lease an additional 12 months, under the same terms as the original lease. (App.186).

The Millville Lease required a security deposit of $2,175 "to assure that the Tenant performs all of the Tenant's obligations under [the] Lease." (App.175). Among other things, the Millville Lease required the tenant to "conduct ordinary maintenance;" pay "for all repairs, replacements and damages caused by the act or neglect of the Tenant;" "repair any damage prior to vacating;" and return the property "in the same condition as it was at the beginning of the Term, except for normal wear and tear." (App.175).

The Millville Lease also set out the terms governing the parties' rights and obligations with respect to the security deposit:

> The Landlord shall inspect the Property after the Tenant vacates at the end of the Term. **Within 30 days of the termination of this Lease, the Landlord shall return the Security Deposit plus the undistributed interest to the Tenant, less any charges expended by the Landlord for damages to the Property resulting from the Tenant's occupancy.** The interest and deductions shall be itemized in a statement by the Landlord, and shall be forwarded to the Tenant with the balance of the Security Deposit by personal delivery, or registered or certified mail.

(App.175) (emphasis added). The Millville Lease declared expressly that "[t]he Security Deposit *may not be used by the Tenant for the payment of rent* without the written consent of the Landlord." (App.175) (emphasis added). And the Millville Lease also prohibited any modification to the lease except "in writing by an agreement signed" by both parties. (App.178).

B. Governor Murphy's COVID-19 Response

New Jersey confirmed its first case of COVID-19 on March 4, 2020. *COVID-19 Confirmed Case Summary*, N.J. Dep't of Health 5 (May 27, 2020), *available at* https://bit.ly/39K28qf. Five days later, on March 9, Governor Murphy issued Executive Order ("EO") 103, declaring a public health emergency and state of emergency in New Jersey. Murphy Exec. Order No. 103 (Mar. 9, 2020), at 1, *available at* https://bit.ly/3gdZCeo.

Governor Murphy would go on to issue over 100 executive orders relating to the pandemic, admitting that he did so without considering the constitutional limits on his power.[1] *See Executive Orders*, The Official Website for the State of New Jersey (last visited June 10, 2021), *available at* https://bit.ly/3cyJfrP. As relevant to this case, Governor Murphy imposed a moratorium on evictions and foreclosures *after* seeking

[1] Anthony Leonardi, *'Above my pay grade': New Jersey governor claims Bill of Rights did not factor into his coronavirus executive orders*, WASHINGTON EXAMINER (Apr. 15, 2020), *available at* https://washex.am/3tKRlTS.

legislative authorization—something he failed to do here. *See* Murphy Exec. Order No. 106 (Mar. 19, 2020), *available at* https://bit.ly/3wUVmr0 (citing N.J. Assembly Bill No. 3859 (2020); N.J. Senate Bill No. 2276 (2020)).

On April 24, 2020, Governor Murphy issued EO 128, the order at issue here. EO 128 mandates that *all* residential housing providers—regardless of the terms of their respective leases, the number of units a housing provider rents, or whether either contracting party suffered a loss of income due to the pandemic—must, upon a tenant's written request, credit their security deposit "towards rent payments due or to become due from the tenant during the Public Health Emergency established in [EO 103] or up to 60 days after the Public Health Emergency terminates." Murphy Exec. Order No. 128 (April 24, 2020), at 3-4 ¶ 1, *available at* https://bit.ly/34XbOv0. "When a tenant applies or credits such deposit, interest, or earnings to pay rent," the housing provider cannot recoup that money and "[t]he tenant shall otherwise be without obligation to make any further security deposit" for the *duration* of the lease. *Id.* at 4 ¶ 2. Even if the parties then extend or renew the lease, the tenant does not have to replenish the security deposit until *six months after* Governor Murphy declares an end to the public health emergency. *Id.*

Despite settled New Jersey law prohibiting an executive order from amending or repealing statutory law, Governor Murphy also purported to "waive[] provisions of statutory law that prohibit the use of security deposits for rental payments, enabling tenants to instruct landlords to use their security deposits to offset rent or back rent."

Press Release, *Governor Murphy Signs Executive Order Providing Critical Short-Term Support for Renters*, Official Site of the State of New Jersey (Apr. 24, 2020), *available at* https://bit.ly/3sTpUaT. Under EO 128's terms, a tenant's "[u]se of a security deposit for the purposes outlined in [EO 128] shall not be considered a violation of N.J.S.A. 46:8-19 et seq." *Id.* at 5 ¶ 3. Governor Murphy further declared that any provisions of New Jersey's Rent Security Deposit Act, N.J.S.A. 46:8-19 *et seq.*, that are inconsistent with EO 128 are no longer in force and effect until 60 days after the end of the Public Health Emergency. *Id.* at 5 ¶ 3.

Remarkably, two of the statutes that Governor Murphy waived forbid exactly what EO 128 tried to accomplish: waiving unwaivable provisions of the Rent Security Deposit Act ("RSDA"). Sections 46:8-24 and -36 mandate that any attempt by a housing provider or tenant to waive the applicability of any provision of the RSDA is void and unenforceable. Thus, the legislature felt so strongly about these mandatory contractual provisions that they prohibited private parties from contracting around them. Yet, Governor Murphy did just that unilaterally and imposed *criminal* penalties on any housing providers that adhere to those statutes and to the terms of their original leases rather than EO 128: "Penalties for violations of [Executive Order 128] may be imposed under, among other statutes, N.J.S.A. App. A:9-49 and -50." *Id.* at 5 ¶ 4.

Rationalizing EO 128, Governor Murphy explained that "many New Jerseyans [are] experiencing substantial loss of income as a result of business closures, reduction in hours, or layoffs related to COVID-19," and that "tenants may be suffering from

one or more financial hardships that are caused by or related to the COVID-19 pandemic, including but not limited to a substantial loss of or drop in income, and additional expenses such as those relating to necessary health care[.]" *Id.* at 2. He proclaimed that it was "plainly in the public interest" to "enabl[e] individuals to pay portions of their rent with the security deposit they own" to "allow those individuals to mitigate the consequences regarding evictions and accumulation of interest and late fees upon termination of Executive Order No. 106 (2020)" because tenants may face "consequences from a late payment of rent, including interest and late fees, which they may be unable to satisfy in light of their substantial loss of income[.]" *Id.* at 3.

According to EO 128, the order would safeguard housing providers' rights because they could supposedly "recoup from the tenant any monies … that would have been reimbursable by the security deposit[.]" *Id.* at 4. Additionally, Governor Murphy made clear that he did not view EO 128 as a taking of property, stating that "pursuant to N.J.S.A. 46:8-19, a security deposit and the accumulated interest and earnings on the investment of such deposit remain the property of the tenant[.]" *Id.* at 3.

C. The Rowan Tenants Invoked EO 128 & Left the Property Damaged

On June 1, 2020, three of the Rowan Tenants handed Mr. Kravitz letters requesting to use their portions of the security deposit ($500 each) to pay rent owed under the Glassboro Lease. (App.188-92). Mr. Kravitz would later discover, however, that the Rowan Tenants caused $1,854.94 in damage to his Glassboro Property.

(App.77). The very purpose of the $2,000 security deposit that the Rowan Tenants agreed to pay was to protect the Kravitzes' property in this exact circumstance, and to allow them to repair any damage to the property without personally incurring the time and expense necessary to recover those costs.

Had Governor Murphy not unilaterally and unlawfully changed the terms of the Glassboro Lease, the $2,000 security deposit would have covered the $1,854.94 in damage that the Rowan Tenants caused to the Glassboro Property. As a direct result of Governor Murphy's unlawful order, the Kravitzes are *still* struggling one year later to track down their former tenants to recover funds needed to repair their damaged property.

D. Appellants Sue to Enjoin Governor Murphy's Unlawful Order

On June 2, 2020, Matthew Johnson[2] sued Appellees in the U.S. District Court for the District of New Jersey, seeking a declaration that EO 128 was unlawful and an injunction against Appellees' enforcement of EO 128. His complaint raised four counts under the U.S. Constitution and four counts under the New Jersey Constitution. (App.85-97).

Twenty-six days later, on June 28, Mr. Johnson filed an unopposed motion to amend his complaint, maintaining all the same substantive allegations but adding Appellants as plaintiffs in the action. (App.45). The trial court granted the motion to

[2] Matthew Johnson is not a party in this appeal.

amend on September 24 (App.207), which led the Appellees to file a motion to dismiss on September 30, asserting that the complaint did not state a federal claim upon which relief could be granted. (ECF No. 26). Appellees also declined to waive sovereign immunity over the related state-law causes of action, prompting the parties to stipulate to the voluntary dismissal of those state-law claims (App.208), which Appellants would later refile in the Appellate Division of New Jersey's Superior Court. *Kravitz v. Murphy*, No. A-1584-20 (N.J. App. Div., argued June 1, 2021).

Appellants opposed the motion to dismiss on several grounds. (ECF No. 36). Preliminarily, they sought to disabuse the trial court of any misconception that the court must turn a blind eye to the legal processes (or lack thereof) that the state used in issuing an order that violates the federal constitution. As Appellants explained, the Appellees' refusal to waive sovereign immunity does not prevent federal courts from considering *ultra vires* state action while assessing a federal cause of action. That the New Jersey Governor acted outside the prescribed constitutional channels, for instance, implicates whether his unilateral executive action is entitled to the same sort of deference that federal courts may otherwise give to the considered legislative judgment of a state legislature. Expanding on this point, Appellants clarified that "[t]he level of deference federal courts afford to such unilateral executive action, as opposed to duly enacted legislation, is a question of federal law[,]" unaffected by the Eleventh Amendment. (App.214)..

Appellants' opposition articulated why EO 128 is the exact type of law that the Contracts Clause forbids. Through his order, Governor Murphy chose economic winners and losers, forcing a disfavored constituency to shoulder an added financial burden to relieve a favored group of its contractual obligations. Applying the Supreme Court's two-part test to EO 128, Appellants showed that Governor Murphy had upset housing providers' legitimate expectations and substantially impaired their leases by retroactively waiving express provisions of their leases, thereby interfering with express contractual obligations and lessening the value of those contracts, in a manner that a court in equity never could. Moreover, Appellants showed, those impairments were not sufficiently tailored to EO 128's stated purpose because, among other things, the order was overly broad and included no means test to ensure that only those tenants in need of relief could take advantage of the order. Nor was EO 128 sufficiently time-limited because its effects were set to linger long after the emergency subsided and will continue to impair residential leases for up to six months after Governor Murphy lifted the public-health emergency.[3]

The trial court dismissed the complaint in its entirety. (App.3, 4). Seeming to misunderstand the Appellants' arguments, the trial court forbid itself from considering the process through which Governor Murphy issued EO 128 (App.24-25) and adopted

[3] Plaintiffs also raised federal claims under the Fourteenth Amendment that they do not press on appeal. For the sake of brevity and clarity, Appellants omit discussion of those claims from this brief.

the reasoning of a federal district judge in New York that "courts '*must* accord substantial deference"' to a state's judgments. (App.27) (quoting *Elmsford Apartment Assocs., LLC v. Cuomo*, 469 F. Supp. 3d 148, 169 (S.D.N.Y. 2020)) (emphasis added). Proceeding with its mistaken belief that the court owed substantial deference to Governor Murphy in its Contracts Clause analysis, the trial court went on to rule that EO 128 did not impair residential leases, almost entirely because New Jersey has previously regulated residential security deposits. (App.29-31). In the trial court's view, Governor Murphy's wholesale rewriting of long-standing New Jersey security-deposit laws—which have protected the contractual rights of parties to residential leases for over a century—should have come as no surprise to residential housing providers because the state had already regulated certain aspects of the use of security deposits. (App.29-31).

Because the trial court decided that EO 128 did not impair residential leases, the court did not consider Governor Murphy's failure to tailor his order to a significant and legitimate public purpose. (App.34).

Appellants noted their timely appeal on April 21, 2021. (App.1).

E. The Legislature Ends the Public-Health Emergency

On June 4, 2021, Governor Murphy signed legislation that required him to end the public-health emergency and most of the executive orders that he issued based on that emergency. N.J. Assembly Bill 5820 (2021); N.J. Senate Bill 3866 (2021).

"Immediately following the signing of the legislation, Governor Murphy signed Executive Order 244, ending the COVID-19 Public Health Emergency." Press Release, *Governor Murphy Signs Legislation and Executive Order Ending COVID-19 Public Health Emergency*, Official Site of New Jersey (June 4, 2021), *available at* https://bit.ly/35e4xGZ. EO 244 declared that, "in light of this legislation becoming law, the Public Health Emergency declared in Executive Order No. 103 (2020) can be safely and responsibly lifted." Murphy Exec. Order No. 244 (June 4, 2021), *available at* https://bit.ly/3zrP7x0.

Because EO 128 stated that it "shall … remain in effect until 60 days following the end of the Public Health Emergency" established by EO 103, residential tenants may seek to rely on EO 128 until August 3, 2021, with the effects of EO 128 lingering long afterward for those housing providers whose tenants have invoked the order.

ARGUMENT

I. THE TRIAL COURT ERRED BY AFFORDING SUBSTANTIAL DEFERENCE TO GOVERNOR MURPHY'S UNILATERAL DECISION TO WAIVE STATE LAW

The Eleventh Amendment does not require federal courts to afford identical treatment to all contract-impairing state laws. It is true that the Supreme Court has permitted courts to defer to the considered judgment of state *legislatures* when considering state action under the Contracts Clause. *See Am. Exp. Travel Related Servs., Inc. v. Sidamon-Eristoff*, 669 F.3d 359, 368-69 (3d Cir. 2012) ("[C]ourts *may* 'defer to legislative judgment as to the necessity and reasonableness of a particular measure.'")

(quoting *U.S. Trust Co. of N.Y. v. New Jersey*, 431 U.S. 1, 19, n.17 (1977)) (emphasis added). But all state action does not get deference—let alone the "substantial deference" the trial court applied to the Governor's edict—as a matter of right whenever it impairs private contracts. The trial court erred both in its Eleventh Amendment analysis and in its decision to afford Governor Murphy substantial deference.

A. EO 128 Was *Ultra Vires*

The trial court misunderstood the Eleventh Amendment inquiry and erred in concluding that sovereign immunity prohibited the court from considering the process by which Governor Murphy enacted EO 128.

Absent a waiver of sovereign immunity, the Eleventh Amendment prevents federal courts from ordering state officials to follow state law. *See Pennhurst State Sch. & Hosp. v. Halderman*, 465 U.S. 89, 101 & n.11 (1984). That typically means that federal courts will not parse the scope of state statutes to declare that a state official exceeded his or her authority under state law in a particular instance. *Id.* But when a state official acts beyond the scope of his or her *constitutional* authority, Eleventh Amendment immunity is unavailable because the official could not have been acting on the state's behalf. *Larson v. Domestic & Foreign Commerce Corp.*, 337 U.S. 682, 689-90 (1949).

More importantly for this case, the Eleventh Amendment imposes *no bar whatsoever* on the federal courts' ascertaining or considering state law in their resolution of federal-law claims. As was the case in *Everett v. Schramm*, federal jurisdiction over

Appellants' claims "was based on the existence of a federal question, not, as in *Pennhurst II*, on principles of pendent jurisdiction." 772 F.2d 1114, 1119 (3d Cir. 1985). Resolving federal questions involving state actors sometimes requires federal courts to ascertain state law—that "is a far cry from compelling state officials to comply with [state law]," which is all the Eleventh Amendment prohibits. *Id.* "The ascertainment of state law is an everyday function of the federal court[;]" otherwise, the Eleventh Amendment would render useless almost any federal cause of action against state officials. *Id.* That federal law—and federal supremacy—might "incidentally require compliance with state law" (or merely deny deference to state actors who fail to abide by state law) does not implicate the Eleventh Amendment. *Id.* A state—or governor—that violates federal law "is no better off because it also violates its own law." *Louise B. v. Coluatti*, 606 F.2d 392, 399 (3d Cir. 1979).

Settled New Jersey law is clear that Governor Murphy lacked *any* authority to amend, waive, or repeal statutory law. *See, e.g.*, *Commc'ns Workers of Am., ALF-CIO v. Christie*, 994 A.2d 545, 564 (N.J. App. Div. 2010) (quoting *Williamson v. Treasurer*, 814 A.2d 1153 (N.J. App. Div. 2003) ("Simply put, an Executive Order cannot amend or repeal a statute.") (citing *Twiss v. Dep't of Treasury*, 571 A.2d 333, 339 (N.J. App. Div. 1990) ("There can be no dispute that neither an Executive Order nor regulation can change or repeal specific statutory authorizations."), *rev'd on other grounds*, 591 A.2d 913 (N.J. 1991)); *see also Accident Index Bureau, Inc. v. Hughes*, 215 A.2d 529 (N.J. 1965) (holding that an executive order cannot limit the application of a statute).

The Governor's lack of power to waive duly enacted statutes is separate in kind from a contention that Governor Murphy exceeded the scope of his claimed source of authority, New Jersey's Disaster Control Act. If Appellants had argued, for instance, that EO 128 was *ultra vires* merely because the Disaster Control Act does not extend to economic emergencies, or does not authorize orders related to residential tenancies, the trial court's Eleventh Amendment analysis might have been correct. The *Elmsford* case on which the trial court relied illustrates this distinction. The plaintiffs in *Elmsford* conceded that New York Governor Cuomo's order at issue was not "itself, unconstitutional." 469 F. Supp. 33d at 162 (quoting the plaintiffs' brief). Given this concession, the Southern District of New York concluded that the plaintiffs were impermissibly asking the court "to police the boundaries of state law" by asking the court to consider "Governor Cuomo's alleged violations of the authority delegated to him by the New York legislature." *Id.* (cleaned up). But that is not this case. Regardless of the contours of the Disaster Control Act and Governor Murphy's statutory power to respond to an emergency, the Governor of New Jersey lacks "any authority whatever" to waive duly enacted statutes. *See Pennhurst*, 465 U.S. 89 at n.11.

Governor Murphy's unilateral waiver of statutory law was outside his constitutional authority and could not have been an action on behalf of the state. *See Larson*, 337 U.S. at 689-90. The trial court, therefore, erred in holding that the Eleventh Amendment prohibited any consideration of "theories based on the idea that

[Appellees] violated [Appellants'] federal Contracts Clause constitutional rights by Governor Murphy's alleged *ultra vires* action." (App.25).

B. Governor Murphy's Unilateral Waiver of State Law Does Not Deserve Deference

The trial court compounded its Eleventh Amendment error by holding that it *must* grant "substantial deference" to Governor Murphy during its Contracts Clause analysis. (App.27). As Appellants pointed out to the trial court, the level of deference that federal courts give the judgment of state actors while considering violations of the U.S. Constitution is purely a question of federal law, unaffected by the Eleventh Amendment. (App.329). Put differently: the Eleventh Amendment prevents a federal court from mandating a state official's compliance with state law—it in no way *requires* a federal court to grant *substantial* deference to a governor's unilateral judgments when analyzing whether that governor impaired private contracts in violation of the federal Contracts Clause.

The idea that federal courts, in applying the Contracts Clause, should defer to a state's legislative judgment "as to the necessity and reasonableness of a particular measure" traces back to *East New York Savings Bank v. Hahn*, 326 U.S. 230 (1945). *See U.S. Trust*, 431 U.S. at 22-23 (citing *Hahn*). The reasoning in *Hahn* confirms, however, that the Court does not simply defer to a state legislature's judgment without considering the legislative process. On the contrary, the Court analyzed the "whole course" of New York's law-making process, which the Court described as "the empiric

process of legislation at its fairest: frequent reconsideration, intensive study of the consequences of what has been done, readjustment to changing conditions, and safeguarding the future on the basis of responsible forecasts." 236 U.S. at 234. The legislature "was not even acting merely upon the pooled general knowledge of its members. … The New York Legislature was advised by those having special responsibility to inform it that 'the sudden termination of the legislation which ha[d] dammed up normal liquidation of [] mortgages for more than eight years might well result in an emergency more acute than that which the original legislation was intended to alleviate.'" *Id.* at 234-35 (quoting the legislative record). Given all the evidence that New York's legislature acted with considered judgment to safeguard residents against a serious danger, the Court refused the plaintiffs' invitation to take judicial notice of conflicting economic data to "reject the judgment of the joint legislative committee, of the Governor, and of the Legislature." *Hahn*, 326 U.S. at 234.

To illustrate the standard of legislative judgment deserving of deference, the Court in *Hahn* contrasted New York's legislative process against that from *Worthen Co. v. Kavanaugh*, 295 U.S. 56, 60 (1935), through which the Arkansas Legislature had shown "studied indifference to the interests of the mortgagee or to his appropriate protection." *Hahn*, 326 U.S. at 234 (quoting *Kavanaugh*). Justice Brandeis, writing for the Court in *Kavanaugh*, admonished the Arkansas Legislature for "put[ting] restraint aside" when impairing the contractual rights of mortgagees. 295 U.S. at 60. According to *Kavanaugh*, the law's overbreadth was evidence that the legislature acted without the considered

judgment worthy of deference. *Id.* at 61. The Arkansas Legislature had not made any serious attempt to tailor its laws to their stated purposes, resulting in an unnecessarily broad impact on private contracts. *Id.* ("There is not even a requirement that the debtor shall satisfy the court of his inability to pay."). Given the excessiveness of the law at issue, the Court refused to defer to such "an oppressive and unnecessary destruction of nearly all the incidents that give attractiveness and value to" the contracts at issue. *Id.* at 62.

Kavanaugh is not a relic of the past, nor did *Hahn* mark some sea-change in the level of deference owed under the Contracts Clause. More recently, in *Allied Structural Steel Co. v. Spannaus*, the Supreme Court again refused to defer to a state's legislative judgment because "there [wa]s no showing in the record … that th[e] severe disruption of contractual expectations was necessary to meet an important general social problem." 438 U.S. 234, 247 (1978). *Hahn* provides for deference to state legislative judgments in appropriate cases, but only when the state can satisfy the standards set by the Court. As a federal district court recognized in another COVID-related case, "the degree of deference" is "influenced by the degree to which" the legislative process met the standard of lawmaking recognized in *Hahn*. *See Baptiste v. Kennealy*, 490 F. Supp. 3d 353, 374 (D. Mass. 2020) ("The degree to which future decisions by elected officials … will deserve and receive deference from the court will be influenced by the degree to which they manifest consideration of the requirements of the Constitution and also of the implications of changed relevant facts.").

States must justify deference from federal courts. Before deferring to a state's judgment in impairing contracts, a federal court needs to scrutinize the "whole course" of the law-making process to determine whether the law at issue resulted from the sort of considered, empirical judgment that deserves deference. This inquiry is not a reflexive one. The federal courts' duty to uphold and apply the U.S. Constitution demands far more than the rubber stamp that the trial court applied in this case.

By its very nature as an executive action, EO 128 resulted from even less considered judgment than the laws denied deference in *Kavanaugh* and *Spannaus*. Not only did Governor Murphy act without the benefit of the pooled, collective knowledge on which the legislative process depends, *see Hahn*, 236 U.S. at 234-35, but he also did not base his decision on any expert opinions or empirical analyses. The "intensive study" and expert reports and legislative committees to which the Court in *Hahn* deferred were completely absent here. *See id.* at 234.

Without evincing any considered judgment, Governor Murphy simply decreed that EO 128 was "plainly in the public interest" because some "tenants may be suffering from one or more financial hardships." EO 128 at 2-3. The logic of EO 128 completely overlooks the hardships that housing providers have also faced due to the pandemic (let alone the added hardships imposed by Governor Murphy), and the order's logic collapses under minimal scrutiny. Governor Murphy proclaimed, without any factual basis, that allowing tenants to pay their security deposit toward rent was necessary to "mitigate the consequences regarding evictions and accumulation of interest and late

fees upon termination" of EO 106. *Id.* at 3. But requiring housing providers to apply security deposits to unpaid rent would not save any tenants from an eviction, because Governor Murphy had *already imposed an eviction moratorium* that he scheduled to keep in place at least as long as EO 128. *See* EO 106; *see also* EO 244 (keeping the eviction moratorium in place until at least January 2022). In other words: EO 128 does nothing to achieve its stated purpose. And the law's overbreadth is further evidence that Governor Murphy acted without the kind of considered judgment that receives deference. *See Kavanaugh*, 295 U.S. at 60-61. This order was instead one man acting *outside* the legislative process.

Governor Murphy circumvented the legislative process and issued EO 128 without any empirical considerations. His personal judgment did not meet *Hahn*'s standard for deference. Federal courts do not owe his unilateral decision any deference whatsoever. The trial court erred by misapplying precedent to hold that it "must accord substantial deference" to Governor Murphy's sole judgment. (App.27).

C. The Trial Court's Granting of Substantial Deference Was Inconsistent with the Independence of the Judicial Office and Judicial Impartiality

The trial court turned the Contracts Clause analysis into an obligatory deference regime under which federal courts no longer scrutinize a state's interference with private contracts. But scrutinizing state interference with contracts is the precise role that the Contracts Clause imposes on the federal judiciary. By granting substantial deference to

Governor Murphy, the trial court effectively abdicated the judicial office and biased the outcome of its deliberations in his favor.

Article III of the Constitution vests "the judicial power of the United States" in the courts and creates the judicial office held by "[t]he judges, both of the supreme and inferior courts." U.S. Const., art. III, § 1. The judicial power includes the authority to decide cases and controversies; a judge's office includes a duty to exercise independent judgment in the interpretation and application of law in each case. *See Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 177 (1803) ("It is emphatically the duty of the Judicial Department to say what the law is. Those who apply the rule to particular cases must, of necessity, expound and interpret the rule."). The judicial office carries with it a duty of independent judgment. *See* James Iredell, To the Public, *N.C. Gazette* (Aug. 17, 1786) (describing the Article III duty of judges as "[t]he duty of the power"). Each judge who holds the judicial office under Article III swears an oath to the Constitution and is duty-bound to exercise his or her own office independently. *See* Philip Hamburger, LAW AND JUDICIAL DUTY 507-12 (2008) (discussing judges' internal duty of independent judgment).

Through the independent judicial office, the Founders sought to ensure that judges would not administer justice based on someone else's interpretation of the law. *See* Max Farrand, 2 THE RECORDS OF THE FEDERAL CONVENTION OF 1787, 79 (1911) (Nathaniel Gorham explaining that "the Judges ought to carry into the exposition of the laws no prepossessions with regard to them"); The Federalist No. 78 (Alexander

Hamilton) ("The interpretation of laws is the proper and peculiar province of the courts."). This obligation of independence is reflected in the opinions of the founding era's finest jurists. *See, e.g.*, *Georgia v. Brailsford*, 2 U.S. 415, 416 (1793) (Iredell, J., dissenting) ("It is my misfortune to dissent … but I am bound to decide, according to the dictates of my own judgment."); *The Julia*, 14 F. Cas. 27, 33 (C.C.D. Mass. 1813) (Story, J.) ("[M]y duty requires that whatsoever may be its imperfections, my own judgment should be pronounced to the parties."); *United States v. Burr*, 25 F. Cas. 2, 15 (C.C.D. Va. 1807) (Marshall, J.) ("[W]hether [the point] be conceded by others or not, it is the dictate of my own judgment, and in the performance of my duty I can know no other guide.").

Judicial independence, as a duty and obligation, persists today. These principles are so axiomatic, in fact, that they seldom appear in legal argument; the mere suggestion that a judge might breach his or her duty of independent judgment or display bias is a scandalous insinuation. But that is exactly what the trial court appears to have done by requiring substantial deference to the Governor's decision to violate the Appellants' rights constitutionally protected by the Contracts Clause. The Governor's opinion of how to best respond to an emergency or exercise the state's police power is a separate and distinct question from whether the response he chose violates the U.S. Constitution. Even in times of crisis, it remains the judiciary's role to construe the limits of constitutional law. *Marbury*, 5 U.S. at 177. The duty of independent judgment is the very office of an Article III judge; a judge cannot fulfill that duty in a Contracts Clause

case by rubber-stamping whatever executive action a governor claims to be in the state's interest. *Cf. United States v. Nasir*, 982 F.3d 144, 177 (3d Cir. 2020) (Bibas, J., concurring) ("Anything less is too narrow a view of the judicial role.").

Substantial deference to state actors in a Contracts Clause case also jeopardizes judicial impartiality, "the *sine qua non* of the American legal system." *Haines v. Liggett Group*, 975 F.2d 81, 98 (3d Cir. 1992); *see also Com. Coatings Corp. v. Cont'l Cas. Co.*, 393 U.S. 145, 149 (1968) (holding that judicial bodies "not only must be unbiased but also must avoid even the appearance of bias."). A neutral judiciary "safeguards the two central concerns of procedural due process, the prevention of unjustified or mistaken deprivations and the promotion of participation and dialogue by affected individuals in the decisionmaking process." *Marshall v. Jerrico, Inc.*, 446 U.S. 238, 242 (1980). By ensuring a neutral arbiter, due process "helps to guarantee that life, liberty, or property will not be taken on the basis of an erroneous or distorted conception of the facts or the law." *Id.*

Moreover, due process requires the federal government to act "through judges whose office required them to exercise independent judgment in accord with the law." Philip Hamburger, IS ADMINISTRATIVE LAW UNLAWFUL? 173 (2014). Judicial bias need not be personal bias to violate the Constitution—it can also be institutional. In fact, institutionalized judicial bias is more pervasive, as it systematically subjects parties across the entire judiciary to bias rather than only a party before a particular judge.

The trial court's Contracts Clause analysis institutionalized bias by *requiring* substantial deference to the Governor's view of his own actions. *Cf.* Philip Hamburger, Chevron *Bias*, 84 GEO. WASH. L. REV. 1187 (2016). Instead of exercising independent judgment about the limits the Contracts Clause imposes on the states, the trial court adopted a rule that systematically biases the federal courts in favor of the Governor—one of the litigants in the case. The state wins simply by proclaiming that the challenged order was necessary and within its police power. No rationale can defend a practice that weights the scales in favor of a *government* litigant—the most powerful of parties. *Cf. Masterpiece Cake Shop, Ltd. v. Colo. Civil Rights Comm'n*, 138 S. Ct. 1719, 1734 (2018) (Kagan, J., concurring) (agreeing that the Constitution forbids adjudicatory proceedings that are "infected by … bias"); *Tumey v. Ohio*, 273 U.S. 510, 532 (1927) ("Every procedure" that might lead a judge "not to hold the balance nice, clear, and true between the State and the accused denies the latter due process of law.").

A requirement of substantial deference to the state is particularly inappropriate given the purpose of the Contracts Clause. As discussed more in Section II, the Contracts Clause exists to provide citizens with a federal venue that will protect their private contracts from undue state interference. *See Edwards v. Kearzey*, 96 U.S. (6 Otto) 595, 605 (1877). The trial court's approach, however, would render that constitutional promise nugatory—skewing the resolution of Contracts Clause cases in the state's favor. This Court should restore the federal judiciary's proper role in the protection of

private contracts against undue state interference. "To hold otherwise would seriously undermine the national government's role[.]" *Everett*, 772 F.2d at 1119.

II. EO 128 VIOLATES THE CONTRACTS CLAUSE

In violation of the Contracts Clause, EO 128 relieved a favored constituency of its contractual obligations at the expense of a smaller and less popular constituency. While the pandemic touched nearly every life nationwide, Governor Murphy determined unilaterally that residential tenants—regardless of demonstrated need—were more deserving of relief than their contractual counterparts. Compounding the problem, he decided that housing providers should personally shoulder the cost of relieving tenants of their voluntarily assumed contractual obligations. A contract is only as good as a party's ability to enforce its obligations. "If the Contract[s] Clause is to retain any meaning at all," *Spannaus*, 438 U.S. at 242, it must prevent state actions like EO 128 that go beyond anything a court in equity could do to nullify express contractual rights and obligations, reverse the parties' incentives, and severely diminish a contract's value.

A. The Purpose & Meaning of the Contracts Clause

When the Founders gathered in Philadelphia during the summer of 1787, they were well acquainted with national emergency. Eight years of revolution caused intense pecuniary distress, made worse by the years under the Articles of Confederation when the federal government lacked any ability to check the overreach of state governments.

Economic precarity became widespread, leading to "an ignoble array of legislative schemes" that interfered with private contracts by relieving favored constituencies of their contractual obligations. *See Edwards*, 96 U.S. at 605. State interference with contracts destroyed the credit of the very constituencies the legislatures had hoped to save and undermined confidence in the economy more broadly. *Id.* State legislatures' "changing the relative situation of debtor and creditor … touche[d] the interest of all." *Ogden v. Saunders*, 25 U.S. (12 Wheat.) 213, 354-55 (1827) (Marshall, C.J.). The problem "had become so great, so alarming, as not only to impair commercial intercourse, and threaten the existence of credit, but to sap the morals of the people, and destroy the sanctity of private faith." *Id.*

The Contracts Clause "was one of the important benefits expected from a reform of the government." *Id.* at 355. With firsthand knowledge of how interference with private contracts could endanger the country, the Founders drafted the new Constitution "[t]o meet these evils in their various phases." *Edwards*, 96 U.S. at 606.

In choosing the terms of the Contracts Clause, "the framers were absolute." *Sveen v. Melin*, 138 S. Ct. 1815, 1821 (2018) (Gorsuch, J., dissenting). James Madison argued that any "'inconvenience' of a categorical rule would, on the whole, 'be overbalanced by the utility of it.'" Douglas W. Kmiec & John O. McGinnis, *The Contract Clause: A Return to the Original Understanding*, 14 Hastings Const. L. Q. 525, 560 & n.24 (1987) (quoting Farrand, at 439). Anything less absolute would be prone to "[e]vasions … devised by the ingenuity of Legislatures." Farrand, at 440.

The Founders agreed to prohibit states from passing "any … Law impairing the Obligation of Contracts." U.S. Const., art. I, § 10. That provision, now known as the Contracts Clause, "applies to *any* kind of contract." *Sveen*, 138 S. Ct. at 1821.

In his public advocacy for ratification, Madison explained that laws impairing contractual obligations "were not only forbidden by the Constitution," "but were 'contrary to the first principles of the social compact, and to every principle of sound legislation.'" *Edwards*, 96 U.S. at 606 (quoting Federalist 44). He assured the public that the Contracts Clause would prevent legislation that retroactively displaced contractual rights. Kmiec, 14 Hastings Const. L. Q. at 532; *see also Reynolds v. McArthur*, 27 U.S. (2 Pet.) 417, 434 (1829) (stating that "laws by which human action is to be regulated, look forwards, not backwards"). The states "chose to ratify the Constitution—categorical Clause and all." *Sveen*, 138 S. Ct. at 1827 (Gorsuch, J., dissenting).

Although "[t]he treatment of the malady was severe, [] the cure was complete." *Edwards*, 96 U.S. at 606. The Contracts Clause restored public confidence in government, "[c]ommerce and industry awoke," and "[p]ublic credit was reanimated. The owners of property and holders of money freely parted with both, well knowing that no future law could impair the obligation of the contract." *Id.* at 606-07 (citation omitted).

Soon after the states ratified the new Constitution, the Supreme Court recognized that the Contracts Clause's purpose was "to establish a great principle, that contracts should be inviolable[.]" *Sturges v. Crowninshield*, 17 U.S. (4 Wheat.) 122, 205

(1819) (Marshall, C.J.). Acknowledging the categorical prohibition against retroactive interference with contractual obligations, Chief Justice John Marshall wrote that the Court should give the clause its "full and obvious meaning" because the Constitution's plain text should give way to "extrinsic circumstances" only if "the absurdity and injustice of applying the provision to the case[] would be so monstrous[] that all mankind would, without hesitation, unite in rejecting the application." *Id.* at 202-03, 205-06. For the next hundred years or so, the Supreme Court continued to "carry out the intent of contracts and the intent of the Constitution[,]" reasoning that "[t]he obligation of the former is placed under the safeguard of the latter." *Edwards*, 96 U.S. at 607; *see also Bronson v. Kinzie*, 42 U.S. (1 How.) 311, 318 (1843) ("[I]t would but ill become this court, under any circumstances, to depart from the plain meaning of the words used" in the Contracts Clause.).

During the New Deal era, however, the Court in *Blaisdell* questioned the Court's continued adherence to the Contracts Clause's original meaning, ruling that a more lenient standard would apply to state laws that altered the remedies available to enforce contracts. *See Home Bldg. & Loan Ass'n v. Blaisdell*, 290 U.S. at 442-43. That decision was more bark than bite, though. As the Court explained the next term, even before *Blaisdell* a state was "free to regulate the procedure in its courts even with reference to contracts already made … , and moderate extensions of the time for pleading or for trial will ordinarily fall within the power so reserved." *Kavanaugh*, 295 U.S. at 60. Only laws that retroactively impaired contractual rights or obligations run afoul of the

Contracts Clause. *See, e.g.*, *McCracken v. Hayward*, 43 U.S. (2 How.) 608, 612 (1844). This remedy/obligation distinction mattered because, according to the Court, a contracting party is more likely to expect (and, therefore, price into the contract) that the laws governing contractual remedies might change than to expect the state to retroactively alter contractual obligations. *See, e.g.*, *U.S. Trust*, 431 U.S. at 19 n.17. Because *Blaisdell* dealt only with the modification of remedies, the case had nothing to say about state interference with contractual obligations and, therefore, did not overrule over a century of precedent constraining state interference with obligations. *Cf. Sveen*, 138 S. Ct. at 1822 (reasoning that the statute at issue, which altered obligations, "stack[ed] up well against laws that th[e] Court upheld against Contracts Clause challenges as far back as the early 1800s"). Laws that retroactively impair contractual obligations remain constitutionally suspect.

B. EO 128 Does Not Satisfy the Supreme Court's Contracts Clause Test

When considering a Contracts Clause challenge, courts apply a two-step inquiry, asking: (1) "whether the state law has 'operated as a substantial impairment of a contractual relationship'" and (2) "whether the state law is drawn in an 'appropriate' and 'reasonable' way to advance 'a significant and legitimate public purpose.'" *Sveen*, 138 S. Ct. at 1821-22 (citations omitted). The greater the impairment, the higher "the hurdle the state legislation must clear" at the second step of the inquiry. *Allied Structural*, 438 U.S. at 245. A severe impairment "will push the inquiry to a careful examination

of the nature and purpose of the state legislation." *Id.* But even when the impairment is less severe, a court will not sustain an unreasonable regulation "simply because the [creditors'] rights were not totally destroyed." *U.S. Trust*, 431 U.S. at 27.

1. EO 128 Substantially Impairs Appellants' Contracts

The first step of the Contracts Clause analysis has three components of its own: "whether there is a contractual relationship, whether a change in law impairs that contractual relationship, and whether the impairment is substantial." *Gen. Motors Corp. v. Romein*, 503 U.S. 181,186 (1992). But the first two components often resolve easily, leaving the court to focus on the severity of the impairment. *See id.* That is true here. Appellants' residential leases are contracts that EO 128 impaired by nullifying Appellants' rights to hold security deposits. What remains is a determination that the impairment to Appellants' leases was substantial. *See id.*

The substantiality of state interference turns on "the extent to which the law undermines the contractual bargain, interferes with a party's reasonable expectations, and prevents the party from safeguarding or reinstating his rights." *Sveen*, 128 S. Ct. at 1822. "Total destruction of contractual expectations is not necessary for a finding of substantial impairment." *Energy Reserves Grp. v. Kansas Power & Light Co.*, 459 U.S. 400, 411 (1983). Courts "look to 'the legitimate expectations of the contracting parties,'" to assess whether, "at the time the parties entered into the contract and relied on its terms," they would have expected the modification at issue. *Am. Exp.*, 669 F.3d at 369 (quoting

U.S. Trust, 431 U.S. at 19 n.17). If the law at issue has "substantially thwarted" the plaintiffs' "legitimate expectations," then it has substantially impaired the contract. *Watters v. Bd. of Sch. Directors of City of Scranton*, 400 F. Supp. 3d 117, 133 (M.D. Pa. 2019) (quoting *Transp. Workers Union of Am., Local 290 v. Southeastern Pa. Transp. Auth.*, 145 F.3d 619, 622 (3d Cir. 1998)), *aff'd*, 975 F.3d 406 (3d Cir. 2020).

The Supreme Court has identified several factors that show when an impairment has upset the contracting parties' legitimate expectations:

- The law impairs a contractual right or obligation as opposed to simply modifying the remedies for enforcement available, *U.S. Trust*, 431 U.S. at 19 n.17;
- The contract has "an express covenant" permitting the action that the law now prohibits, *Bronson*, 42 U.S. at 320-21; *see also Spannaus*, 438 U.S. at 247 ("[T]he statute in question here nullifies express terms of the company's contractual obligations[.]"); *U.S. Trust*, 431 U.S. at 19 n.17 (reasoning that "a law adjusting the express terms of an agreement" is more likely to upset expectations);
- The law changes a contract in a way that a court could not have done through its equitable power, *Sveen*, 138 S. Ct. at 1823 (reasoning that a divorce court has wide discretion to divide property in the way the new law did); *Kavanaugh*, 295 U.S. at 63 (distinguishing *Blaisdell* because "[t]here has been not even an

attempt to assimilate what was done by this decree to the discretionary action of a chancellor in subjecting an equitable remedy to an equitable condition"); *cf. Blaisdell*, 290 U.S. at 446 (reasoning that a court in equity could impose similar conditions on foreclosure);

- The change in law "lessen[s] the value of the contract," *Edwards*, 96 U.S. at 601, 607 ("One of the tests that a contract has been impaired is[] that its value has by legislation been diminished."); *Green v. Biddle*, 21 U.S. (8 Wheat.) 1, 75-76 (1823) ("[C]onditions and restrictions tending to diminish the value and amount of the thing recovered, impairs [the plaintiff's] right to, and interest in, the property."); *see also U.S. Trust*, 431 U.S. at 19 ("[T]he State has made no effort to compensate the bondholders for any loss sustained by the repeal."); *Blaisdell*, 290 U.S. at 432-34 (relying on the fact that the law compensated creditors during the extended redemption period);
- The law changes the incentive structure created by the contract, *Kavanaugh*, 295 U.S. at 60-61; or undermines the parties' reliance interests, *Spannaus*, 438 U.S. at 246 ("Not only did the state law thus retroactively modify the [compensation scheme], but also it did so by changing the company's obligations in an area where the element of reliance was vital[.]");
- The law does not provide the impaired party with an opportunity to restore their rights under the contract, *compare Sveen*, 138 S. Ct. at 1823 ("[A]

policyholder can reverse the effect of the Minnesota statute with the stroke of a pen."); *with Spannaus*, 438 U.S. at 250 ("It did not effect simply a temporary alteration of the contractual relationships … but worked a severe, permanent, and immediate change in those relationships—irrevocably and retroactively."); and

- Prior regulation in the industry would not have caused the contracting parties to expect the future change in regulation, *Energy Reserves Grp.*, 459 U.S. at 411 ("In determining the extent of the impairment, we are to consider whether the industry the complaining party has entered has been regulated in the past."); *Veix v. Sixth Ward Building & Loan Ass'n of Newark*, 310 U.S. 32 (1940) ("When he purchased into an enterprise already regulated in the particular to which he now objects, he purchased subject to further legislation upon the same topic.").

At least the first six of these seven factors support the conclusion that EO 128 substantially impaired the Appellants' contracts. A security deposit was an obligation that Appellants included as an express provision in their contracts. As the Millville Lease explained, the security deposit was "to assure that the Tenant performs all of the Tenant's obligations under [the] Lease." (App.175). The Glassboro and Millville Leases both specified that the tenants could not use their security deposits toward rent payments. (App.175). And the Sixth Street Lease stated explicitly that the Johnsons would return the security deposit *only* "on the full and faithful performance of the lease."

(App.175). Not only were these terms explicit in Appellants' leases, but the Millville Lease also prohibited any attempts to change the terms of the lease or to waive the requirements of applicable statutory law. (App.175). By negating the effect—and criminalizing the enforcement—of these express covenants, Appellees substantially impaired Appellants' contracts. *See Bronson*, 42 U.S. at 320-21.

The trial court got the remedy/obligation inquiry backward. (App.32). Focusing on contractual remedies rather than obligations, the court relied on the fact that EO 128 "does not displace the civil remedies available." (App.32). But, as the Supreme Court has held and Appellants made clear in their briefing below, an alteration of contractual *obligations* is the change more likely to upset the parties' expectations. *See U.S. Trust*, 431 at 19 n.17. Whether remedies remained nominally in place is of little consequence, considering reasonable modification of contractual remedies "is much less likely to upset expectations than adjusting the express terms of an agreement[,]" *id.*, and states typically remain "free to regulate the procedure in [their] courts even with reference to contracts already made[.]" *Kavanaugh*, 295 U.S. at 60. The trial court's reliance on the availability of remedies is even more puzzling considering that the very purpose of a security deposit is to allow housing providers to protect their property *without* resorting to any available remedies.

Moreover, no court in equity could have required Appellants (or any other residential housing provider in New Jersey) to give up the security for which they expressly contracted—particularly without even the slightest individualized showing

that their tenants needed such relief. *See id.* at 63. The Supreme Court in *Sveen* recently held that a change in Minnesota law could not have upset the parties' reasonable expectations because, by changing the default life-insurance beneficiary in case of divorce, the law had done no more than divorce courts routinely do through their discretionary, equitable power. 128 S. Ct. at 1823. And in *Blaisdell*, the legislature limited the contractual impairment to the courts' equitable authority. *See* 290 U.S. at 416-18. To take advantage of the temporary change in law in that case, mortgagors had to prove to a court that it was "just and equitable" to extend their redemption periods.[4] *Id.* EO 128 stands in stark contrast to such limited impairments. Governor Murphy made no "attempt to assimilate what was done by this decree to the discretionary action of a chancellor in subjecting an equitable remedy to an equitable condition." *Kavanaugh*, 295 U.S. at 63. Consequently, housing providers like Appellants could not have expected such a retroactive impairment of their contractual rights.

EO 128 also changed the parties' incentives under the contracts, as well as the

[4] Moreover, the Court in *Blaisdell* stressed that the Minnesota law did not upset the creditors' expectations because they were "predominantly corporations, such as insurance companies, banks, and investment and mortgage companies" whose "chief concern" is protecting a financial investment. *Id.* at 445-46. Because the law did not diminish their eventual ability to realize the proceeds of that investment, there was no substantial impairment. *Id.* By contrast, Appellants are local property owners who lease only one or two units, the rental income on which they rely to pay their own bills. They depend on the security deposits to protect against physical damage likely to occur when they lease their property, because having to recoup damages increases the cost to Appellants and slows their ability to relet the property. EO 128 criminalized any efforts to assert the rights for which they freely contracted, and which had been specifically secured by statute.

Appellants' reliance interests. In *Kavanaugh*, decided the term after *Blaisdell*, the Supreme Court struck down a series of state laws that created a six-and-a-half-year waiting period during which the holder of a mortgage could not recover possession of a property from a delinquent owner. 295 U.S. at 59-61. The Court reasoned, "Under the statutes in force at the making of the contract, the property owner was spurred by every motive of self-interest to pay his assessments if he could, and to pay them without delay." *Id.* at 60. But under the statute at issue, the property owner "ha[d] every incentive to refuse to pay a dollar, either for interest or for principal." *Id.* at 60-61.

A similar change in incentives resulted here. Take the Rowan Tenants for example. Under the terms of the Glassboro Lease, the Rowan Tenants leased the property for one year, in exchange for $2,000 per month in rent, plus an added $2,000 as security for the Kravitzes. (App.141-42). If the Rowan Tenants did not clean the property or repair any damage before vacating, they agreed that the Kravitzes could deduct those costs from their security deposit. (App.142). But because EO 128 required the Kravitzes to accede to the Rowan Tenants' request to apply their security deposit to pay the final month's rent (App.188-92), the order perverted the contract's incentives and allowed the Rowan Tenants to leave the property in disrepair without any immediate consequence for them. (App.77). Had the $2,000 deposit remained in place, the Rowan Tenants would have had to choose between cleaning and repairing the property themselves or forfeiting their $2,000, just as the contract contemplated. But EO 128 created "every incentive" for them to apply their security deposit toward

their last month's rent, forcing the Kravitzes to shoulder the cost of $1,854.95 in damages—a cost they have still not been able to recoup. *See Kavanaugh*, 295 U.S. at 295.

By depriving Appellants of their security deposits, EO 128 diminished the value of their contracts. *See Edwards*, 96 U.S. at 601, 607. Appellants contracted for a deposit amounting to between 8% and 12.5% of their respective leases' value, to secure their private property against damage. Although these deposits technically remained the tenants' property, the Appellants could hold that money in escrow to protect against any damage that might occur during the tenancy. Had the Appellants known they could not keep a security deposit to ensure that their tenants would cover any cost of repairs, the Appellants could have mitigated their risk another way—such as by raising the monthly rent. In this way, EO 128 changed the value of the contracts that the Appellants had negotiated. *See Green*, 21 U.S. at 75-76.

Worse yet, EO 128 did all this without any attempt to make the Appellants whole or compensate them for their diminished rights. The *Blaisdell* decision on which Appellees relied below hinged on the fact that the law at issue compensated the creditors by requiring the debtors to pay rent during the time the law extended the mortgage-redemption period. *See* 290 U.S. at 445-46. The Supreme Court later emphasized that it would have invalidated the law in *Blaisdell* "had [it] not possessed the characteristics attributed to it by the Court." *Spannaus*, 438 U.S. at 242. According to the Court, these limitations on *Blaisdell* were clear from "three cases that followed closely in *Blaisdell*'s wake[,]" *id.* at 243, including *Kavanaugh*, which struck down a law

that did not condition relief "upon payment of interest and taxes or the rental value of the premises." 295 U.S. at 61; *see also U.S. Trust*, 431 U.S. at 19 ("[T]he State has made no effort to compensate the bondholders for any loss sustained by the repeal.").

Finally, EO 128 imposed a permanent change on the residential leases it impaired. Like most residential leases, Appellants' contracts included a one-year term. EO 128 has already remained in effect for longer than that year. And, by its terms, EO 128 remains in effect for *longer* than the duration of a lease once a tenant invokes the order: "When a tenant applies or credits such deposit, interest, or earnings to pay rent," the home provider cannot recoup that money and "[t]he tenant shall otherwise be without obligation to make any further security deposit" for the duration of the lease. EO 128 at 4 ¶ 2. Even if the parties extend or renew the lease, the tenant does not have to replenish the security deposit until *six months after* Governor Murphy declares an end to the public-health emergency. *Id.* (emphasis added).

The trial court seemed to think that the eventual availability of civil litigation to recoup what EO 128 had cost the Appellants meant that EO 128 allowed Appellants to restore their rights under the contract. (App.33). But that rationale misses the point. Appellants did not contract for the right to hold their tenants liable for damage to the property—that right already existed. Instead, Appellants contracted for the right to hold a security deposit in escrow from which they could deduct the cost of any damage, thereby avoiding the need to pursue civil litigation and enabling to property to be relet immediately. EO 128 does not allow housing providers to restore *that* right. *See*

Spannaus, 438 U.S. at 250 ("It did not effect simply a temporary alteration of the contractual relationships of those within its coverage, but worked a severe, permanent, and immediate change in those relationships—irrevocably and retroactively.").

Disregarding the six factors that favor a finding that EO 128 substantially impaired Appellants' contracts, the trial court erroneously gave nearly dispositive weight to the prior-regulation factor—without even contemplating those factors that undermined its view. Worse, the trial court did not consider how the seventh factor might have affected the Appellants' legitimate expectations. Rather than considering whether New Jersey's prior regulation of security deposits might have caused Appellants to expect the type of change that Governor Murphy imposed on their contractual rights, the trial court adopted a seemingly blanket rule that will undermine contractual rights in *every* industry subject to any regulation at all.

The trial court's reliance on prior regulation was so strong, in fact, that states could now nullify express obligations in nearly any contract in any industry that is subject to some prior regulation. But the constitutional inquiry focuses on whether the contracting party expected the change in the law. It simply cannot be the case that the mere existence of some regulation puts every contracting party on notice of every conceivable way the law might change, no matter how drastic or substantial the change. *See Elliott v. Bd. of Sch. Trs. of Madison Consol. Schs.*, 876 F.3d 926, 936 (7th Cir. 2017) (reasoning that whether the parties anticipated "*retroactive application* to impair existing contract rights and reliance interests [wa]s another question").

A look at New Jersey's prior regulation of security deposits illustrates the problem with the trial court's overreliance on past regulation as an indicator of the parties' future expectations. Housing providers in New Jersey have freely contracted for security deposits for well over a century. *See Hecklau*, 59 A. at 18. The legislature passed the Rent Security Deposit Act in 1968 "to protect tenants from overreaching landlords who require[d] rent security deposits from tenants and then divert[ed] such deposits to their personal use." *Watson v. Jaffe*, 296 A.2d 537, 537 (N.J. App. Div. 1972). Since then, the law regulating security deposits has remained quite stable, with *statutory* amendments focusing on technical matters like the type of bank account the deposit must be kept in, the interest it must bear, and what happens to the deposit in case of foreclosure or sale. *See, e.g.*, N.J.L. 1971, c.233 (requiring, *inter alia*, deposit to be held in an interest-bearing account and applying statute to providers with only two rental units); N.J.L. 1973, c.195 (increasing escrow requirements and adding penalties for non-compliance); N.J.L. 1985, c.42 (further specifying escrow requirements and simplifying the process in case of foreclosure).

In short, there have been seven modest amendments to security-deposit regulations in over 50 years. These changes could not conceivably have put Appellants on notice that the Governor might one day unilaterally and retroactively nullify and criminalize their longstanding right to maintain a security deposit. *See Elliott*, 876 F.3d at 936. EO 128 did not merely subject Appellants to a tad bit more regulation; it unwound years of legislation, reliance interests, and contractual expectations with one

lawless stroke of the pen. No housing provider in New Jersey could have expected a change so sweeping and diametrically opposed to the history of security-deposit legislation. In fact, considering the importance of certainty in the property-rights context, it was shocking that the Governor would even claim such power.

Because EO 128 has altered express terms of Appellants' contracts, changed the incentive structure that those contracts put in place, lessened the value of the contracts, and diminished Appellants' rights thereunder, the impairment is substantial.

2. EO 128 Is Not an Appropriate or Reasonable Way of Achieving Its Stated Purpose

Given the substantial impairment of Appellants' contracts, Appellees must clear an even higher hurdle to survive scrutiny. *Spannaus*, 438 U.S. at 245. Appellees must prove that the impairment that EO 128 caused to Appellants' contracts was "both necessary and reasonable to meet the purpose advanced by the [state] in justification." *U.S. Paper & Forestry Rubber Mfg. Allied Indus. & Serv. Workers Int'l Union v. Gov't of V.I.*, 842 F.3d 201, 211 (3d Cir. 2016). This Court's review is "more exacting than the rational basis standard applied in the due process analysis." *Am. Exp.*, 669 F.3d at 369; *see also Alarm Detection Sys., Inc. v. Village of Schaumburg*, 930 F.3d 812, 823 (7th Cir. 2019) ("There is no presumption of legislative validity under the Contracts Clause, and it demands more than a legitimate end and a rational means."); *Ass'n of Equip. Mfrs. v. Burgum*, 932 F.3d 727, 735 (8th Cir. 2019) (same). The Governor must "demonstrate more than a conceivable or incidental public purpose for impairing the obligation of

contracts." *Burgum*, 932 F.3d at 734. An impairment is unreasonable when "an evident and more moderate course would serve [the state's] purposes equally well." *U.S. Trust*, 431 U.S. at 21; *see also Spannaus*, 438 U.S. at 247 (analyzing whether an impairment "was necessary to meet an important general social problem").

a. EO 128 Does Not Serve a Legitimate Public Purpose

EO 128 does not promote a legitimate public purpose because it does nothing to achieve either of its stated purposes. According to Governor Murphy, EO 128 was "plainly in the public interest" because it would help mitigate evictions during the pandemic. But Governor Murphy had already issued an eviction moratorium, one which preceded EO 128 and will remain in place longer. *See* EO 106; EO 244. Requiring housing providers to apply security deposits toward rent does not help tenants avoid eviction when they cannot be evicted in the first place. It also does nothing to decrease any back rent a tenant may owe if that tenant has not damaged the property. Those tenants who leave the property in good repair remain free to negotiate with housing providers to apply their security deposit toward any past-due rent.

Moreover, a law impairing contractual rights *must* benefit the public generally rather than just a discrete group. *Energy Reserves Grp.*, 459 U.S. at 412; *see also Spannaus*, 438 U.S. at 242 (explaining that the law in *Blaisdell* did not offend the Contracts Clause, in part, because it "was enacted to protect a basic societal interest, not a favored group"). "Since *Blaisdell*, the Court has reaffirmed that the Contract[s] Clause prohibits

special-interest redistributive laws, even if the legislation might have a conceivable or incidental public purpose." *Burgum*, 932 F.3d at 732 (citation omitted). Laws with incidental public benefits violate the Contracts Clause if the benefit is targeted at a specific constituency. *See, e.g.*, *id.* at 733 ("The law primarily benefits a particular economic actor in the farm economy—farm equipment dealers. Even if the law indirectly might benefit farmers and rural communities, the Contract Clause demands more than incidental public benefits."); *Equip. Mfrs. Inst. v. Janklow*, 300 F.3d 842, 859-61 (8th Cir. 2002) (same).

In *Spannaus*, for instance, the Court struck down a law altering pensions, which despite seeming generally applicable on its face, could "hardly be characterized … as one enacted to protect a broad societal interest rather than a narrow class." *Id.* at 238, 248-49. The law "applie[d] only to private employers who" met certain extremely specific requirements. *Id.* at 248. This targeted relief failed to satisfy the broad public purpose required by the Contracts Clause.

Not only does EO 128 benefit only residential tenants, but the order helps them at the expense of housing providers—not through the general public coffers. Political favoritism at the expense of a disfavored group is the exact behavior the Framers drafted the Contracts Clause to prevent. *See* Laurence Tribe, American Constitutional Law, § 9-8, p. 613 (2d ed. 1988) (The Contracts Clause serves to protect minority rights "from improvident majoritarian impairment."). That the public includes more tenants

than housing providers does not transform the order's political favoritism into a general public purpose.

The ongoing emergency does not change this analysis. "Emergency does not increase granted power or remove or diminish the restrictions imposed upon power granted or reserved." *Blaisdell*, 290 U.S. at 425. The Framers were acutely aware of crises of "unprecedented pecuniary distress" when they drafted the Contracts Clause. *Edwards*, 96 U.S. at 604. Many Contracts Clause cases have struck down legislation enacted in the face of crises. *See, e.g.*, *Kavanaugh*, 295 U.S. at 60; *Bronson*, 42 U.S. 311. This Court should likewise declare that EO 128 violates the Contracts Clause.

b. Governor Murphy Did Not Tailor EO 128 to Its Stated Purpose

EO 128 also fails because Governor Murphy did not make any attempt to tailor his order in the ways that have allowed some other state laws to survive scrutiny under the Contracts Clause. Broad contractual impairments cannot survive when "a less drastic modification" would have achieved the legislative purpose while limiting the impairment of contractual rights. *See U.S. Trust*, 431 U.S. at 30. "[A] state is not free to impose a drastic impairment when an evident and more moderate course would serve its purposes equally well." *Id.* at 31.

The *Blaisdell* decision is instructive on how narrowly tailored a law must be to survive scrutiny. The Court identified three ways the law was tailored to a narrow state interest: the law (1) provided only "temporary and conditional" relief, (2) was "sustained because of [an] emergency," and (3) provided for reasonable compensation while the

law impaired creditor's rights. 290 U.S. at 441-42. Although the foreclosure moratorium in *Blaisdell* diminished the mortgagees' contractual remedies, the impairment was for a finite period, and the law compensated mortgagees until they could eventually enforce their rights. *Id.* at 416, 445-46. And as explained above, all the tailoring described in *Blaisdell* was vital to the Court's upholding of the law at issue. *See Spannaus*, 438 U.S. at 242-43.

No similar tailoring took place here. For one, EO 128 has no temporal limit. Tenants can take advantage of EO 128 for 60 days after the conclusion of the public-health emergency on which Governor Murphy relied and *after* their leases have expired. And if impairing year-long contracts for 16 months were not damaging enough, Governor Murphy structured EO 128 so that, once a tenant invoked the order, EO 128 would govern the parties' contractual relationship for the duration of the lease, *plus* an additional six months after the emergency, if the parties renewed their lease (a likely outcome considering the eviction moratorium).

Nor is EO 128 tailored to those in need of aid. Given the lack of any input from the legislature and its pooled knowledge, it is unsurprising that Governor Murphy failed to consider "an evident and more moderate course [that] would serve [the state's]

purposes equally well." *See U.S. Trust*, 431 U.S. at 21.[5] Crucially, Governor Murphy did not include any means test or mechanism to limit EO 128's relief to only those tenants who are "suffering from one or more financial hardships that are caused by or related to the COVID-19 pandemic[.]" EO 128 (emphasis added). The foreclosure moratorium in *Blaisdell*, for example, authorized a court to extend the redemption period only when doing so was "just and equitable." 290 U.S. at 416, 445. In fact, the Court distinguished the law at issue from the *Bronson* case, in which the Court struck down a law that gave unconditional relief to debtors. *Id.* at 432; *see also Kavanaugh*, 295 U.S. at 61 ("There is not even a requirement that the debtor shall satisfy the court of his inability to pay.").

Further, nothing in EO 128 compensates Appellants for the diminished value of their contracts. *See Blaisdell*, 290 U.S. at 442 ("[P]rovision was made for reasonable compensation to the landlord during the period he was prevented from regaining possession."). Instead, Appellants must now pay out of pocket to cover the cost of damage to their property, hoping to eventually recover those costs through civil litigation—a process which includes its own added costs, assuming the housing

[5] For instance, California tailored its tenant-assistance legislation by requiring tenants to declare under penalty of perjury swearing that they have suffered a hardship because of COVID-19, and the law also includes specific protections for housing providers with four or fewer units. State of California, *Tenant, Homeowner, and Small Landlord Relief and Stabilization Act of 2020*, *available at* https://bit.ly/3wv1VBe.

provider can even track down the former tenant to serve them. *See Green*, 21 U.S. at 75-76.

* * *

EO 128 violates the Contracts Clause because it substantially impairs the Appellants' contracts and is not an appropriate way of achieving its stated purpose. *See Sveen*, 138 S. Ct. at 1821-22. As Appellants have shown, EO 128 lacks any of the tailoring that the Supreme Court has identified as necessary for contract-impairing state laws to survive constitutional scrutiny. *See, e.g.*, *Blaisdell*, 290 U.S. at 441-42. The trial court, however, distorted the Contracts Clause analysis to such a degree that the constitutional provision no longer provides a check on state power, as it was specifically designed to do. To the extent that this Court agrees with the trial court that *Blaisdell*'s progeny has extended so far as to negate any reasonable expectation that contracts in regulated industries remain free from state interference, Appellants maintain that such case law is contrary to the original purpose an understanding of the Contracts Clause and should be overruled. (ECF No. 36, n.3).

Appellants rightfully relied on their contracts and their faith that federal courts would ensure that their contracts would remain free from state interference. Nothing in New Jersey security-deposit law defeated that legitimate expectation. Any decision upholding EO 128 conflicts with the Contracts Clause's plain text and purpose and cannot stand.

CONCLUSION

Through EO 128, Governor Murphy unilaterally restructured residential leases in tenants' favor. He interfered with contracts on behalf of a favored constituency, which is precisely what the Contracts Clause prohibits. Because EO 128 substantially impairs Appellants' contracts, it must fail. Appellants ask this Court to reverse the judgment below.

June 16, 2021

Respectfully,

/s/ Jared McClain

NEW CIVIL LIBERTIES ALLIANCE
JARED MCCLAIN
MARK CHENOWETH
RICHARD A. SAMP
HARRIET HAGEMAN
KARA ROLLINS
1225 19th St. NW, Suite 450
Washington, DC 20036
(202) 869-5210
Jared.McClain@NCLA.legal
Counsel for Appellants

REQUEST FOR ORAL ARGUMENT

Appellants request oral argument to help this Court more fully develop and clarify the issues and facts in this case.

CERTIFICATE OF BAR MEMBERSHIP

I, Jared McClain, certify that I am a member of the bar for the United States Court of Appeals for the Third Circuit.

Respectfully,

/s/ Jared McClain
Jared McClain
New Civil Liberties Alliance

CERTIFICATE OF COMPLIANCE

I certify that this brief complies with the requirements of Federal Rule of Appellate Procedure 32(a)(5) and (6) because it has been prepared in 14-point, plain, roman-style font. This brief also complies with the type-volume limitations of Federal Rule of Appellate Procedure 32(a)(7). This brief contains 12,993 words.

I further certify that the electronic version of this brief was scanned with Trend Micro Antivirus. It contains no known viruses.

Respectfully,

/s/ Jared McClain
Jared McClain
New Civil Liberties Alliance

CERTIFICATE OF SERVICE

I hereby certify that I electronically filed Appellants' Opening Brief & Appendices with the Clerk of the Court for the United States Court of Appeals for the Third Circuit by using the appellate CM/ECF system on June 16, 2021. Participants in the case who are registered CM/ECF users will be served by the CM/ECF system.

Respectfully,

/s/ Jared McClain
Jared McClain
New Civil Liberties Alliance
1225 19th Street NW, Suite 450
Washington, D.C. 20009
(202) 869-5210
Jared.McClain@NCLA.legal