REAL PROPERTY

The Constitutionality of Retroactive Legislation and Covid-19 Business Interruption Insurance

By Dennis C. Valet

Business owners looking to their commercial policies for business interruption and loss of income coverage due to Covid-19 have likely run into a giant roadblock — an exclusion of loss caused by virus or bacteria.

Virus exclusions have led practitioners scratching their heads for novel legal theories to find coverage for Covid-19 business interruption where coverage is expressly denied. The New York State Assembly took notice of these exclusions, and the resulting lack of coverage and drafted Assembly Bill A10226A. The bill construes all policies insuring against loss of use and occupancy and business interruption "to include among the covered perils under that policy, coverage for business interruption during a period of a declared state emergency due to the coronavirus disease 2019 (Covid-19) pandemic." It also declares all virus exclusions null and void, and extends this special coverage for the duration of New York's declared state emergency.

Most importantly, the bill is retroactive — deemed effective March 7, 2020 and applying to policies in effect on that date.

Alarm bells are ringing in general counsel offices. Is this even constitutional? After all, the bill will create, in insurers' minds, an unfunded liability that was not bargained for when they set insurance premiums for policies in effect on March 7, 2020.

Article 1 of the United States Constitution provides that "No State shall…pass any… Law impairing the Obligation of Contracts" and the Fifth and Fourteenth Amendments to the United States Constitution prohibit the taking of property without due process of law. In the past insurers have turned to both arguments when objecting to legislation that retroactively imposed new obligations. Long story short, the United States Supreme Court has held that the Constitution permits contractual interference pursuant to a balancing test that evaluates the following factors, to wit: (1) the extent of the interference, (2) the historic regulation of the industry affected by the law, (3) the legitimate public purpose for the law, and (4) whether the law is appropriate given the stated public purpose, with special deference given to laws addressing emergencies.[1] Litigation is inevitable and it appears that the Assembly has specifically drafted this bill with previous case law in mind.

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The New York State Court of Appeals has addressed retroactive insurance coverage legislation in two important decisions.

In *Health Insurance Association of America v. Harnett*[2], the Court of Appeals struck down legislation that required retroactive coverage for maternity care in health insurance policies, doing so on the narrow ground that those policies were forced renewals, where the insurer could not unilaterally cancel or refuse to renew a policy after its period expired, and therefore they did not consent to the change in the substance of the policy. The Court of Appeals did recognize that the legislation could work in other circumstances, stating "while there was a genuine, identifiable public purpose to be served by the enactment of [the law], the predicament which spawned the legislation had not risen to the magnitude of a crisis which warranted overriding the terms of the agreements entered into by the parties." Contrasting the holding in *Harnett*, commercial policies affected by this bill are not automatically renewable and can be cancelled by the insurer. Further, the Assembly bill specifically references the fact that Covid-19 is a state emergency.

In *American Economy Insurance Co. v. State of New York*,[3] the Court of Appeals upheld legislation that insurers argued retroactively imposed unfunded workers' compensation liability. The legislation did away with a special fund that was used to pay for workers' compensation claims that were closed but unexpectedly reopened many years later. This holding was on the narrow ground that the legislation did not change the actual legal enforceability of the contract between insurer and insured, only how the liability was paid for (i.e., passing the cost of the claim from the fund directly to the insurers). Here, the Assembly bill creates a type of fund (although it seems more like a surcharge) that pays for the coverage imposed by retroactive changes, a provision that presumably is intended to bring the bill closer to, rather than further away from, what is permitted by *American Economy Insurance Co.* and *Health Insurance Association of America v. Harnett*, which caution against the rewriting of contractual obligations between insurer and insured.

Other state courts have attempted similar legislation. In *Harleysville Mutual Insurance Co. v. State of South Carolina*[4], the South Carolina Supreme Court struck down a law that retroactively changed the definition of an "occurrence" on the ground that it altered the contractual relationship between insurer and insured without addressing a pressing emergency. In *Vesta Fire Insurance Corp. v. State of Florida*, legislation was permitted that limited property insurance cancellations in the wake of Hurricane Andrew. Likewise, in *State of Louisiana v. All Property & Casualty Insurance Carries Authorized and Licensed to Do Business in State*, the Louisiana Supreme Court upheld legislation that extended the filing deadlines for claims, and the statute of limitations for insurers suing their insurers, in the wake of Hurricanes Katrina and Rita.

So, is the proposed legislation constitutional? There are good arguments for both sides. On one hand, Covid-19 is undoubtedly an emergency and the proposed legislation serves a legitimate and pressing public purpose. The bill even attempts to fund the surprise liability imposed. On the other hand, the bill substantially changes the rights and obligations bargained for when the insurer issued policies in effect on March 7, 2020. It takes a specific and purposeful exclusion and renders it null and void. This ham-fisted approach may prove too much, with particular consideration given to whether there are less invasive solutions available to the legislature.

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1. *Home Building & Loan Association v. Blaisdell*, 290 US 398 (1934) and *Energy Reserves Group, Inc. v. Kansas Power and Light Co.*, 459 US 400 (1983).
2. 44 NY2d 302 (1978).
3. 401 S.C. 15 (2012).
4. 937 So2d 313 (La. 2006).