



Bankruptcy, Workouts and Creditors' Rights Law Alert

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The modernization of Ohio's receivership statute

I. Introduction

Effective March 23, 2015, Ohio's antiquated receivership statute (Ohio Rev. Code Chapter 2735) will be modernized, particularly as it relates to the appointment of a receiver in commercial mortgage foreclosures and the ability of a receiver to sell real estate free and clear of liens.

II. Appointment of a receiver

Previously, commercial mortgagees were a bit hamstrung because only two of Ohio Rev. Code Section 2735.01's provisions for appointment of a receiver typically potentially applied: Section 2735.01(B) ("In an action by a mortgagee, for the foreclosure of his mortgage and sale of the mortgaged property, when it appears that the mortgaged property is in danger of being lost, removed, materially injured, or that the condition of the mortgage has not been performed, and the property is probably insufficient to discharge the mortgage debt"); and Section 2735.01(F) ("In all other cases in which receivers have been appointed by the usages of equity"). In situations where it was unclear whether the property was worth less than the unpaid mortgage balance, some courts struggled with the decision of whether to appoint a receiver, even in cases where the borrower agreed in the mortgage to appointment of a receiver upon the occurrence of an event of default and without regard to the value of the property. Although in recent years many courts used such contractual language to hold that the borrower waived the operation of Section 2735.01(B)'s valuation requirement, and many courts appointed receivers pursuant to Section 2735.01(F) in instances where the mortgage called for the appointment of a receiver upon an event of default but did not contain any language waiving the valuation requirement, the revised statute removes any doubt about the situations in which a receiver can be appointed.

Section 2735.01 has been re-written and re-numbered, and the new counterpart to old Section 2735.01(B) – Section 2735.01(A)(2) – now provides that a receiver may be appointed:

- (2) In an action by a mortgagee, for the foreclosure of the mortgagee's mortgage and sale of the mortgaged property, when it appears that the mortgaged property is in danger of

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being lost, removed, materially injured, diminished in value, or squandered, or that the condition of the mortgage has not been performed, and **either** of the following applies:

- (a) The property is probably insufficient to discharge the mortgage debt.
- (b) The mortgagor has consented in writing to the appointment of a receiver.

Emphasis added.

The effect of this change is to make it even more clear that the court can appoint a receiver if the mortgage calls for it, even if the property being foreclosed is arguably worth more than the mortgage debt.

In addition, a new Section 2735.01(A)(3) has been added to the statute, and provides that a receiver may be appointed to enforce a contractual assignment of rents and leases. Thus, even if a commercial mortgage fails to contain an agreement for the appointment of a receiver upon default, the lender can obtain appointment of a receiver if the mortgage contains an assignment of rents and leases.

Section 2735.01(F) remains, but is now Section 2735.01(A)(7).

Importantly, Section 2735.01 now distinguishes between receivers appointed over a particular piece of property – such as a parcel of commercial real estate – and “general” receiverships, where the receiver is appointed to operate and/or liquidate the affairs of a business. Section 2735.01(B) makes it clear that if a receiver is appointed under Section 2735.01(A)(1) (appointment of a receiver in an action by a vendor to vacate a fraudulent purchase, in an action involving a dispute among partners with respect to the property, and other similar situations), (2), (3) or (5) (after judgment, to dispose of the property according to the judgment, or to preserve the property pending an appeal, or to force the sale of property by a judgment debtor), he/she is appointed only with respect to the specific property that is the subject of the underlying action. On the other hand, if the receiver is appointed under Section 2735.01(A)(6) (when a company has been dissolved, is insolvent or is in imminent danger of insolvency, or has forfeited its corporate or other entity rights), the receiver may be appointed to manage all the affairs of the company.

Finally, Section 2735.01(D) provides that a receiver appointed under Section 2735.01(A)(4) (to carry a judgment into effect) or (A)(7) may be appointed as to all of the affairs of the entity, or only as to particular property, as determined by the court.

III. Powers of a receiver

Previously, Ohio Rev. Code Section 2735.04 provided merely that:

Under the control of the court which appointed him, as provided in section 2735.01 of the Revised Code, a receiver may bring and defend actions in his own name as receiver, take and keep possession of property, receive rents, collect, compound for, and compromise demands, make transfers, and generally do such acts respecting the property as the court authorizes.

Although the flexibility provided by such general language was often helpful, it sometimes lead to pitched legal battles, as was the case with respect to a receiver’s ability (or inability) to sell real estate free and clear of liens.

Oftentimes, when a receiver desired to sell real estate free and clear of liens, the receiver would be met with resistance from the borrower/debtor, the receiver’s title insurance agent, or both, on the basis that the only procedure under Ohio law for the sale of real estate free and clear of liens was Ohio’s foreclosure statute (Ohio Rev. Code Chapter 2329, et seq.), as a result of which a receiver’s sale had to comply with the requirements of that statute, such as (1) a sale by auction only, (2) an appraisal by three appraisers, (3) a sale for no less than 2/3 of the appraised value, (4) a notice of sale required to be published in a newspaper of general circulation, and (5) a right of redemption by the debtor. Although the courts (and title companies) seemed to warm up to the idea of receiver sales free and clear of liens after the credit meltdown

of 2008 so long as anyone with an interest in the real estate was given prior notice of the proposed disposition and an opportunity to object, title companies remained leery of insuring receiver sales where a party objected to the sale, but the court overruled the objection and allowed the sale to proceed. Accordingly, the revised statute should bring welcome clarity to the circumstances under which a receiver may sell real estate free and clear of liens.

Section 2735.04(B) now sets forth with some particularity the types of actions a receiver may take. More specifically, it provides as follows:

- (B) Under the control of the court that appointed the receiver as provided in Section **2735.01** of the Revised Code, the receiver may do any of the following:
 - (1) Bring and defend actions in the receiver's own name as receiver;
 - (2) Take and keep possession of real or personal property;
 - (3) Collect rents and other obligations, and compromise demands;
 - (4) Enter into contracts, including, but not limited to contracts of sale, lease, or, so long as existing lien rights will not be impacted, contracts for construction and for the completion of construction work;
 - (5) Sell and make transfers of real or personal property;
 - (6) Execute deeds, leases, or other documents of conveyance of real or personal property;
 - (7) Open and maintain deposit accounts in the receiver's name;
 - (8) Generally do any other acts that the court authorizes.

However, Section 2735.04(D) takes that particularity to a whole new level with respect to the sale of property free and clear of liens, setting forth a number of procedural safeguards that will help ensure the sale brings a good price under the circumstances and otherwise comports with the dictates of procedural due process. First, Section 2735.04(D)(1) provides some general tenets for such sales:

- (D)
 - (1)
 - (a) Subject to the approval and supervision of the court and the requirements of this section, a receiver may sell property free and clear of liens by private sale pursuant to a written contract between the receiver and the prospective purchaser, by private auction, by public auction, or by any other method that the court determines is fair to the owner of the property and all other parties with an interest in the property, is reasonable under the circumstances, and will maximize the return from the property to the receivership estate, taking into account the potential cost of holding and operating the property.
 - (b) Before entering an order authorizing the sale of the property by the receiver, the court may require that the receiver provide evidence of the value of the property. That valuation may be provided by any evidence that the court determines is appropriate. In a public or private auction, the court may establish a minimum bid.
 - (c) If the receiver requests authority to sell the property pursuant to a prospective purchase contract and if warranted by the circumstances, the court may require that the receiver solicit and consider additional offers. If the receiver ultimately sells the property to a party other than the original proposed purchaser, if approved by the court, the receiver may pay to the unsuccessful original

proposed purchaser a reasonable amount of costs and expenses from the sale proceeds in an amount determined by the court to compensate that proposed purchaser for participation in the sale process to the extent that participation brought value to the receivership.

Thereafter subsection (2) of Section 2735.04(D) details the specific prerequisites for a sale free and clear of liens, such as the requirement that the receiver (or first mortgage holder) file a motion requesting that the receiver be permitted to sell the property, and that the motion set forth whether the receiver has received a specific offer for which he/she seeks approval, and if so, the identity of the buyer and the proposed sale terms, and if not, the proposed procedures for the conduct of the sale. The sale proponent is also required to provide at least 10 days' prior written notice of the sale pursuant to the Rules of Civil Procedure to all parties to the action and any other persons the title commitment filed in connection with the case identifies as potentially having an interest in the property, and if any such party or person objects to the motion within the required time period, the court must schedule a hearing on the motion. Further, any sale order issued by the court constitutes a final appealable order.

Section 2735.04(D)(3) then provides that if the court finds it to be in the best interest of the receivership estate to sell the property, the court may order such a sale, subject however, to the lien of the county treasurer for real estate taxes and assessments, and that upon the recording of the receiver's deed, the liens shall be cancelled as to the real property and transferred to the sale proceeds with the same priority as they previously attached to the property.

Importantly – especially to title insurers – Ohio Rev. Code Section 2735.04(D)(4) provides that a receiver's sale of real property under subsection (D)(2) is in lieu of a foreclosure sale under Rev. Code Chapter 2329, and that except for the requirement that the sale proponent procure foreclosure title work in connection with the sale, the provisions of Rev. Code Chapter 2329 do not apply.

The new statute also provides, in subsection (5) of Section 2735.04(D), that if the contemplated sale is under division (D)(2)(a)(ii) – one to a specific buyer pursuant to the terms set forth in the sale motion – no separate confirmation order is required. Conversely, subsection (6) provides that if the sale was made under division (D)(2)(a)(i) (at the time of filing of the motion the sale proponent had not received a specific offer acceptable to him/her) the sale proponent is required to file a motion seeking confirmation of the sale. However, even though no motion for confirmation is required in connection with a sale to the specific buyer outlined in the sale motion, Ohio Rev. Code Section 2735.04(D)(10) requires the receiver to file and serve upon all parties and lien holders (not that there should be any lien holders who aren't already parties in the case...) a certificate and report of sale as soon as “reasonably possible” after delivery of the deed to the buyer, certifying the following information:

- (a) That the sale was conducted in accordance with the order authorizing the sale
- (b) The date of the sale
- (c) The name of the purchaser
- (d) The purchase price
- (e) The amount of the net proceeds of the sale after payment of all expenses associated with the sale
- (f) A copy of the closing statement, if a closing statement was prepared
- (g) Any other information that the court may require

Subsections (7) and (8) of Section 2735.04(D) set forth the procedure for redemption by the debtor. Subsection (7) requires the court's order approving the motion to sell free and clear of liens to establish the date by which the debtor must exercise the equity of redemption, which date can be no less than 3 days after entry of the order approving the sale motion.



Subsection (8), in turn, sets forth that the redemption amount is equal to the greater of the sale price or the total unpaid balance of all liens on the property, including interest, costs and other amounts secured by the liens through the redemption date, and also sets forth the procedure for the setting aside of the sale and the transfer of liens to the redemption payment to the receiver.

Finally, Rev. Code Section 2735.04(D)(9) provides for delivery of a deed by the receiver upon closing, and states that the deed has the same effect as a sheriff's deed, namely that it is prima facie evidence of the legality and regularity of the sale and vests in the purchaser all of the interest the debtor had in and to the property.

Time will tell whether the revised statute has any significant shortcomings. At first glance, however, it appears to be a significant improvement over prior law and should bring more structure and predictability to the process of receiver sales of real estate free and clear of liens.

For more information please contact [Jim Botti](#) or any member of Porter Wright's [Bankruptcy, Workout and Creditors' Rights Practice Group](#).

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