

IT IS SO ORDERED.

Dated: 04:37 PM November 17 2009



**UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION**

IN RE:)	CASE NO. 09-53636
)	
ONTARIO LAND COMPANY,)	CHAPTER 11
)	
DEBTOR.)	JUDGE MARILYN SHEA-STONUM
)	
)	OPINION ON ORDER GRANTING MOTION
)	TO ASSUME LEASE OR EXECUTORY
)	CONTRACT [docket #79]

This matter is before the Court on the Debtor’s Motion to Assume Lease or Executory Contract [docket #79] (“Motion”) filed by Ontario Land Company (“Ontario” or “Debtor”), and an objection filed by The Home Savings and Loan Company of Youngstown, Ohio (“Home Savings”) [docket #87]. The Court held a hearing on this matter on November 16, 2009. Appearing at the hearing were Howard Mentzer, counsel for Debtor; and Richard Thomas, counsel for Home Savings.

This proceeding arises in a case referred to this Court by the Standing Order of Reference entered in this District on July 16, 1984. It is determined to be a core proceeding pursuant to 28 U.S.C. § 157(b)(2)(A), over which this Court has jurisdiction pursuant to 28 U.S.C. § 1334. Based upon the arguments of counsel and testimony provided at the November 16, 2009 hearing and the

pleadings on file, the Court makes the following findings of fact and conclusions of law.

I. BACKGROUND FACTS

1. Ontario filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code on August 16, 2009 (the “Petition Date”).

2. Ontario owns, among other properties, a residential subdivision known as Arlington Place. Home Savings financed the purchase of the raw land that is being developed into Arlington Place. The assets of the Debtor include real estate parcels which are raw land and contract rights and other assets unique to real estate holdings.

3. Ontario is engaged in the business of subdividing raw land into residential real estate lots and installing infrastructure improvements on those lots. Upon developing the lots at issue in the present case, Ontario will sell the improved lots to an affiliated developer, K Hovnanian Developments of Ohio, Inc. (“K. Hovnanian”) when the developer has an end purchaser.

4. The Debtor’s ownership of Arlington Place is subject to the senior liens of Home Savings. Home Savings also holds senior liens on other residential subdivisions that Ontario owns, including Villas of Stone Creek, Landings, Fields 2, and MR Village.

5. On September 18, 2009, Debtor filed a Motion for an Order Granting Authority for Sales of Property for Modified Prices and Release Values [docket #37] (“September 18 Motion”). The Debtor, through the September 18 Motion, sought to lower the sales price per lot to K. Hovnanian on 20 different types of improved lots situated in a total of 15 different residential subdivisions. The 15 different residential subdivisions affected by the September 18 Motion are subject to the first liens of seven different lenders.

6. Both Home Savings and FirstMerit Bank, N.A. filed objections to the September 18

Motion. No other parties filed objections to the September 18 Motion.

7. The Debtor resolved the objections of FirstMerit Bank, N.A. and Home Savings by setting agreed release prices for certain lots. The Debtor and Home Savings did not reach an agreement for a release price on the 62' lots in Arlington Place. The parties memorialized the agreed release prices in the Order Granting Authority for Sales of Property for Modified Prices and Release Values, which the Court signed on October 2, 2009 [docket #57].

8. On October 21, 2009, the Court entered an interim order that allowed Debtor to obtain debtor-in-possession financing from K. Hovnanian in order for the Debtor to make infrastructure improvements to raw land in Arlington Place (“DIP Financing Agreement”) [docket #76].

9. The Debtor sought to use the funds that it obtained from the DIP Financing Agreement to improve 12 out of 139 total undeveloped lots in Arlington Place. As a condition of the DIP Financing Agreement, as approved by this Court, K. Hovnanian was granted a priming lien, which will incrementally attach only to those 12 lots and only to the extent that the lots in Arlington Place are actually improved by funds from the DIP Financing Agreement.

10. On November 12, 2009, this Court entered an order [docket #89] and opinion [docket #88] making final the October 21, 2009 interim order for the DIP Financing Agreement.

11. Home Savings will continue to have a first lien on the majority of the unsold lots and raw land at Arlington Place. In addition, Home Savings will have a second lien on the lots that are improved with the DIP Financing proceeds.

12. On October 27, 2009, the Debtor filed the Motion. In the Motion, the Debtor specifically seeks to assume the Lot Option Agreement, originally dated August 1, 2005, as amended,

between the Oster Construction, Inc.¹ and K. Hovnanian Oster Homes, LLC. The Lot Option Agreement, as originally executed, covered approximately 2,900 lots. At the November 16, 2009 hearing, the Debtor's President stated that he believed the current number of lots subject to the Lot Option Agreement is between 1,500 and 1,800 lots.

13. Home Savings filed an objection to the Motion [docket #87] arguing that assuming the Lot Option Agreement is an abuse of the sound business judgment of the Debtor.

II. DISCUSSION

Subject to certain exceptions, none of which apply in this case, "a trustee, subject to the court's approval, may assume or reject any executory contract or unexpired lease of the debtor." 11 U.S.C. § 365(a). A debtor in possession has nearly all of the same rights and powers as a trustee serving in a Chapter 11 case. 11 U.S.C. § 1107(a). One of those powers is the power to assume or reject executory contracts. The primary issue before this Court is whether the Debtor's management has exercised appropriate business judgment in seeking to assume the Lot Option Agreement.

If a debtor assumes a pre-petition contract, the contract is effectively converted into a post-petition contract, so that both the debtor and the contracting party can still compel the other to perform. *Phar-Mor, Inc., et al. v. Strouss Building Associates*, 204 B.R. 948, 951 (N.D. Ohio 1997). A debtor generally will assume only favorable pre-petition contracts. *Id.* The determination as to whether a contract is favorable or not is based upon the debtor's sound business judgment. *Id.* at 951-52 (citing *Lubrizol Entcs., Inc. v. Richmond Metal Finishers, Inc.*, 756 F.2d 1043, 1046-47 (4th Cir. 1985), *cert. denied*, 475 U.S. 1057, 106 S. Ct. 1285 (1985)).

The Court in *Phar-Mor* dealt with a debtor who wished to reject an executory contract, and

¹Oster Construction, Inc. changed its name to Ontario Land Company on August 10, 2009.

stated “[c]ourts should generally defer to a debtor’s decision whether to reject an executory contract.” *Id.* (citing *Lubrizol*, 756 F.2d at 1047). If a court should defer to a debtor’s decision whether to reject an executory contract, then it follows that a court should defer to a debtor’s decision to accept an executory contract – provided that the debtor is exercising sound business judgment.

To determine whether a debtor exercised sound business judgment in its decision to assume or reject an executory contract, “the bankruptcy court should presume that the debtor-in-possession acted prudently, on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the bankruptcy estate.” *Agarwal v. Pomona Valley Med. Group, Inc. (In re Pomona Valley Med. Group, Inc.)*, 476 F.3d 665, 670 (9th Cir. 2007). This Court does, however, require the debtor-in-possession to outline the analysis that informed its business judgment.

Home Savings argues that Ontario was not exercising its business judgment by deciding to sell improved lots to only one developer - K. Hovnanian. However, this Court finds the testimony of Mr. Oster, the Debtor’s President, compelling. K. Hovnanian is a reputable national homebuilder, and one of only two such homebuilders with operations in Northeast Ohio. It has the capacity to purchase, and build homes on, lots in the quantity that Ontario is improving. While the Debtor may be able to sell a few lots on a piecemeal basis, which is what would likely occur if the Debtor offered its improved lots to other small builders, that is not the business model the Debtor has chosen. The Debtor’s choice appears supported by the fact that the administrative costs would likely be higher and the amount of time required to move the lots out of Debtor’s inventory could be much longer. Mr. Oster also testified that there may be the risk of having unfinished homes in a residential subdivision if a small builder were to go out of business prior to completing the construction of a home; the Debtor’s business model greatly minimizes the risk of such a blight on its developments.

The Court raised the issue of the timing of the assumption of the Lot Option Agreement now, as compared to it being addressed in the Debtor's reorganization plan. The Debtor noted the desirability of having K. Hovnanian's continued commitment to the various developments clarified as it proceeds with its plan negotiations with its various lenders. At least seven different lenders have liens on the lots subject to the Lot Option Agreement. The Lot Option Agreement does not impair the liens of any of these lenders. As the Debtor prepares its Chapter 11 Plan, it is beneficial for both the Debtor and the estate that a level of certainty exists.

Because the Court finds Mr. Oster's testimony regarding the reasoning behind the Debtor's business model and the decision to assume the contract at the present time deserving of deference, the Court does not find that the Debtor abused its business judgment. Accordingly, this Court authorizes the Debtor to assume the Lot Option Agreement.

III. CONCLUSION

Based upon the foregoing the Court finds that Ontario's Motion to Assume Lease or Executory Contract is well taken and such motion is hereby GRANTED.

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cc (*via* electronic mail):

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