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Florida Law on Assignment of Rents Provisions

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A recent bankruptcy decision from a New Jersey Bankruptcy Court (*In re Surma*, 504 B.R. 770 (Bankr. D.N.J. 2014)) has once again drawn attention to the effect assignment of rents provisions in mortgages can have, depending on which state's law governs. In *Surma*, the court interpreted an absolute assignment of rents provision contained in a mortgage in light of the interplay between New Jersey state law and the Bankruptcy Code. The court held that because under New Jersey law an absolute assignment of rents passes title to the rents to the assignee, rents generated by property owned by the debtor were property of the lender. Therefore, the rents were not available to fund the debtor's chapter 11 bankruptcy plan.

Assignment of Rents Under Florida Law

Unlike many states, Florida has a statute that governs assignment of rents provisions. An assignment of rents provision may be set forth within a mortgage, or in a separate instrument. *See Fla. Stat.* § 697.07 (the "Rents Statute"). The Rents Statute makes clear in several places that an assignment of rents provision is "security for repayment"[1], that a mortgagee "hold[s] a lien on the rents[2]", and that "enforcement of its assignment of rents under [the Rents Statute] shall not operate to transfer title to any rents not received by the mortgagee".[3] Thus, Florida law is clear that even if a mortgage or separate assignment of rents document contains an assignment of rents provision which purports to be "absolute and not merely as additional security," title to rents does not pass to a mortgagee upon execution of the mortgage, nor upon mere enforcement of rights under the Rents Statute.

The Rents Statute has been described as a "statutory framework under which a mortgagee in a foreclosure action can seek interim relief"[4] in a foreclosure action. In order to invoke this statutory framework, it is critical that a mortgagee make a written demand that the mortgagor "turn over all rents in the possession or control of the mortgagor at the time of the written demand or collected thereafter (the "collected rents") to the mortgagee less payment of any expenses authorized by the mortgagee in writing."[5] A proper written demand for rents is crucial, as the failure to do so has resulted in a mortgagee not being entitled to enforce its lien on rents.[6] In connection with a foreclosure action and pending final adjudication of the same, a state court will typically require the payment of rents less expenses related to the protection and preservation of the mortgaged property either directly to the lender, or into the registry of court.[7] If a mortgagee does receive moneys pursuant to the Rents Statute, it is required to apply them in accordance with the applicable loan documents.[8] Finally, the remedies provided by the Rents Statute "are in addition to any other rights or remedies of the mortgagee or mortgagor under the mortgage, separate assignment of rents instrument, promissory note, at law, or in equity."[9] Therefore, other remedies such as the invocation of a lock box, or directing tenants to remit rents directly to the lender, may still be exercised if appropriate.

One of the interesting aspects of the Rents Statutes relates to when title to rents passes, and thus whether or not rents may be considered a debtor's cash collateral in a bankruptcy case. Although the Rents Statute and cases interpreting it uniformly hold that an assignment of rents provision creates merely a lien on rents that may be enforced, certain courts have permitted the transfer of title to rents to occur prior to a foreclosure sale taking place; specifically, if a final judgment of foreclosure provides that title to rents passes to the mortgagee (prior to the sale taking place), the entry of that judgment has been held to constitute a transfer of title, which

precludes rents from constituting cash collateral.[10] It is also possible that some bankruptcy courts applying Florida law would hold that any "preliminary or final adjudication of the mortgagee's rights"[11] by a state court as to rents could result in rents not being considered cash collateral. Therefore, many cautious bankruptcy practitioners file bankruptcy petitions prior to the entry an order holding that a mortgagee is entitled to possession of rents, not merely prior to a foreclosure judgment being entered, or a foreclosure sale taking place.

Another rents issue that is specific to Florida given its adoption of the Rents Statute is that hotel revenues are *not* considered rents that are subject to the operation the Rents Statute. Rather those revenues are personal property governed by Florida's version of Article 9 of the Uniform Commercial Code, which is found in chapter 679 of the Florida Statutes.[12]

Lessons for Lenders and Servicers

The lessons taught to lenders and services by the Rents Statute and the cases interpreting the same are: (1) upon the occurrence of an event of default, be sure to include a written demand for turnover of rents; (2) do not assume that because your mortgage contains an "absolute" assignment of rents that the lender has title to the rents; that is not the case in Florida; (3) the Rents Statute does not provide the *exclusive* remedy for lenders as to rents; other remedies, such as lock box provisions, may still be utilized in appropriate situations; and (4) the sooner a preliminary or final adjudication as to a mortgagee's rights to rents can be obtained in state court, the less likely it will be that rents will be available to a debtor as cash collateral in a bankruptcy case. As always, every situation and set of loan documents tends to be unique, so review of the loan documents and consultation with counsel is of the utmost importance.

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[1] *Fla. Stat.* § 697.07(1).

[2] *Fla. Stat.* § 697.07(2).

[3] *Fla. Stat.* § 697.07(7).

[4] *In re C & C Dev. Group, LLC*, 2012 WL 171595 (Bkrtcy. S.D. Fla. 2012)

[5] *Fla. Stat.* § 697.07(3).

[6] *Ginsberg v. Lennar Florida Holdings, Inc.*, 645 So.2d 490 (Fla. 3d DCA 1994).

[7] *Fla. Stat.* § 697.07(4).

[8] *Fla. Stat.* § 697.07(8).

[9] *Fla. Stat.* § 697.07(6).

[10] *See In re Villamont-Oxford Assocs., Inc.*, 230 B.R. 445 (Bkrtcy. M.D. Fla. 1998); *In re Venice-Oxford Assocs., Inc.*, 236 B.R. 791 (Bkrtcy. M.D. Fla. 1998).

[11] *Id.*

[12] *In re Ashoka Enterprises, Inc.*, 125 B.R. 845 (Bkrtcy. S.D. Fla. 1990).