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# US Regional Real Estate

Ohio

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## Law and Practice

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## 1. GENERAL

### 1.1 Main Substantive Skills

Necessary substantive skills for lawyers handling sophisticated commercial real estate transactions include:

- knowledge of applicable real estate law, including federal, state and local laws, rules, and regulations;
- understanding of related areas of law, including zoning and entitlements, tax structuring, entity selection and joint ventures, environmental, construction and public and private financing; and
- experience in structuring and negotiating sophisticated real estate transactions.

In recent years real estate law has become increasingly localized and subject to regulation. Those looking to become involved with Ohio properties should understand local markets and players, as well as area law developments and government policies. In addition, COVID-19 makes it essential to maintain a current knowledge of local, state and federal laws and rules impacting real estate.

### 1.2 Most Significant Trends

Some general trends are noted below, although many successful projects may buck them in certain circumstances.

- Industrial/warehouse – demand for new light industrial/warehouse products across Ohio remains robust, resulting in low vacancy and strong fundamentals.
- Residential – the multi-family sector in Ohio has been healthy for several years, but the COVID-19 pandemic has caused some flight to single-family residential housing, driving up residential prices. The recent large inventory in Ohio’s major cities – including Cleveland, Cincinnati and Columbus – helped normalize

rents on multi-family assets, and we’ve seen some deceleration in market fundamentals. It remains to be seen whether this trend will continue in the post-pandemic era.

- Retail – Ohio’s retail and restaurant sectors generally track with the national decline in retail, with many stores suffering from online shopping competition. Some enclosed malls and other retail centers have been shuttered or converted. Nationally, dozens of major retailers declared bankruptcy during the pandemic, exacerbating these pressures.
- Office – Ohio’s office sector remains relatively stagnant. Despite stable job growth, we’ve not seen a significant corresponding increase in new office space development. The pandemic is driving users to remote work arrangements, thus reducing office space demand. Tenants increasingly want smaller leased and owned facilities to lower operating costs, and they prefer buildings providing efficiency, flexibility and key amenities.

Recent deals include the following.

- Columbus Crew (Major League Soccer Team), Columbus – constructed and developed a USD300 million soccer stadium and related facilities; included cooperative arrangements with the City of Columbus, Franklin County and Ohio state agencies.
- The Foundry, Cincinnati – transformation of the former Macy’s store at downtown Fountain Place into a USD50 million-plus commercial and office building with street-level retail space and a glass façade.
- Sherwin Williams, Cleveland – the “paint giant” acquired a key piece of land at Public Square and announced the construction of a 1 million-square-foot office tower for its international headquarters.
- The Lumen, Cleveland – a luxury apartment tower across from downtown’s Playhouse Square.

- Beulah Place, Grove City – a USD350 million mixed-use development, replacing a 220-acre horseracing track facility.
- Hillcrest Solar project, Greater Cincinnati – a USD200-million facility that will double the state’s installed solar capacity.

### 1.3 Impact of New US Tax Law Changes

The Tax Cuts and Jobs Act (TCJA), effective December 2017, had a positive impact on corporate earnings and commercial real estate investments. The legislation reduced the corporate income tax rate to a flat 21% and the effective income tax rates for certain non-corporate taxpayers also fell.

TCJA also stipulated:

- retention of 1031 exchanges for real property not held primarily for sale;
- retention of the maximum capital gains rate at 20%;
- retention of low-income housing tax credits, new markets tax credits and the 20% historic tax credit for qualified historic structure rehabilitation; and
- elimination of the alternative minimum corporate tax.

## 2. SALE AND PURCHASE

### 2.1 Ownership Structures

Ohio recognizes several ownership structures that may hold legal title, including corporations and limited liability companies, as well as individuals, general partnerships, limited partnerships and limited liability partnerships. See **5. Investment Vehicles**.

Under state law, when title is held by an individual, that person’s spouse automatically acquires rights of “dower.” When the owner sells or mortgages real estate, the spouse must

join in the execution of the deed or mortgage to release dower rights. Additionally, a “trust” isn’t a legal entity capable of holding title; rather, title may be held by a person or company acting as trustee for the trust. Two exceptions are Real Estate Investment Trusts (REITs) and “business trusts,” in which the beneficiaries hold transferable shares of beneficial interests in the trust.

### 2.2 Important Jurisdictional Requirements

Certain disclosures are required in residential real estate transactions. In sales of property containing one-to-four dwelling units, sellers must provide buyers with a Residential Property Disclosure Form that reveals property condition defects. Some transactions are exempt, including sales by court order, among co-owners or family members, or of newly constructed residential real estate. Sellers’ failure to provide the disclosure forms gives buyers the right to rescind contracts.

Federal law requires disclosure of lead-based paint in the sale or lease of residences constructed before 1978. No similar disclosure requirements apply to sales of commercial, industrial and other non-residential properties.

### 2.3 Effecting Lawful and Proper Transfer of Title

Transfers of title require parties to file deeds in county auditors’ offices. Auditors transfer ownership on tax records and collect transfer taxes (as described in **2.10 Taxes Applicable to a Transaction**). Next, deeds are recorded in county recorders’ offices.

Properties legal descriptions must meet certain standards for deeds to be accepted for transfer and recording. Property splits must comply with applicable subdivision requirements.

It is advisable to submit proposed new legal descriptions to county engineers' offices for advance approval.

## 2.4 Real Estate Due Diligence

Real estate due diligence in Ohio generally mirrors that in other states. The major steps include:

- reviewing title to the real estate, typically by obtaining a commitment for title insurance;
- obtaining a property survey;
- conducting an environmental assessment;
- conducting inspection of the building and its major components, like the foundation, roof and building systems;
- obtaining soil reports and analysis of applicable governmental requirements for land to be developed;
- reviewing the status of zoning and permits to confirm the intended use is lawful; and
- for income-producing property, reviewing financial reports and leases and confirming the status of commercial leases by obtaining estoppel certificates from tenants.

## 2.5 Typical Representations and Warranties for Purchase and Sale Agreements

Sellers of residential properties with one-to-four dwelling units are required to provide a Residential Property Disclosure Form describing the property's condition.

### Commercial Transactions

In commercial transactions, representations and warranties vary widely and are subject to negotiation. They typically include statements regarding the sellers' authority to complete transactions and representations of "off-record title matters," which are non-public-record issues that could affect title to real estate. These concerns include:

- whether any work has recently been performed on a property that could give rise to a mechanic's lien;
- whether any of the property has been leased or other possessory rights have been granted;
- whether known encroachments of buildings across boundary lines exist;
- whether any lawsuits have been threatened; and
- whether the seller has knowledge of any pending or proposed governmental actions, such as a condemnation or zoning change.

### Environment

Environmental provisions of commercial purchase agreements vary widely and are subject to negotiation. Many sellers insist on sales in "as-is" condition and allow buyers full rights to property inspection, but provide no representations or warranties. On the other end of the spectrum, buyers may insist on broad representations and warranties covering environmental matters. Between these extremes, sellers may provide representations limited to actions occurring during their ownership, or limited to sellers' "knowledge," or based on existing environmental reports, which are disclosed to buyers.

### Condition

Some commercial purchase agreements contain representations and warranties regarding property condition, eg, that the seller hasn't received any notices of violation, that the roof and mechanical systems are in good working order, that there are no known defects, etc. More commonly, purchasers receive time to inspect properties and make condition determinations. If purchasers are unsatisfied, they may elect to terminate agreements.

### Sophisticated Transactions

In more sophisticated real estate transactions, it's common for parties to negotiate limitations on amounts of potential liability and timeframes

within which breaches of representations and warranties may be claimed.

## Residential Transactions

Residential sales provide a statutory right of rescission for misrepresentations in the Residential Property Disclosure Form. This right expires either 30 days after purchase offer acceptance or sale closing date, whichever is earlier.

## 2.6 Important Areas of Law for Foreign Investors

Non-US investors should carefully consider the type of entity that will hold title to real estate, because the choice has both tax and liability implications. For example, a pass-through entity may avoid taxation at the corporate level. Limited liability companies and corporations are used to retain liability at the entity level, providing a shield against investor liability.

Ohio mandates a reporting requirement for non-US owners of real estate (as described in **2.11 Rules and Regulations Applicable to Foreign Investors**).

Investors should also know how real estate investments are taxed at the federal, state and local levels.

## 2.7 Soil Pollution and Environmental Contamination

Even if property contamination was caused by a prior owner, Ohio laws may make a current owner responsible for the release or threatened release of hazardous substances and hold it strictly liable to both the state and third parties for any necessary clean-up costs. Owners and operators of contaminated property may also be liable to Ohio or other parties for damages.

Environmental risk allocations are negotiated on a case-by-case basis, depending on many circumstances, including knowledge of existing

conditions, party responsible for any historical contamination, planned future development and use, and risk based on prior use. Sellers will generally aim to shift liability to buyers and sell contaminated property on an “as-is” basis, except perhaps when sellers are completing ongoing remediation plans. Buyers may seek to require sellers to retain liability for historical environmental impacts.

## 2.8 Permitted Uses of Real Estate under Zoning and Planning Law

### Zoning Laws

Zoning laws are a matter of public record, and local zoning maps indicate an area’s current zoning category. Zoning codes identify permitted uses and standards that must be complied with, including height restrictions, setbacks and other criteria.

Local governments often provide letters confirming zoning statuses, but these may be very general, so buyers may also obtain zoning endorsements to title insurance policies secured at acquisition.

### Development Agreements

Development agreements generally document governmental inducements for constructing improvements or attracting new business to an area. They serve an important function if local governments agree to provide real estate tax abatement, employment tax abatement, public infrastructure improvements or other incentives.

## 2.9 Condemnation, Expropriation or Compulsory Purchase

In Ohio, a variety of governmental entities hold powers of eminent domain, including the state, counties and cities, as well as park, water and sewer districts. Under state law, governmental bodies first determine that land-takings are necessary, obtain land-value appraisals and make offers based on those prices. If owners contest

the price, governmental entities may file actions to take the land and have courts determine prices. Owners may dispute land values in court proceedings.

Owners sometimes challenge original determinations that takings are necessary, but courts tend to give legislative authorities considerable discretion in determining need.

Condemnation actions are commonly used to establish or widen public streets or install water or sewer lines or similar infrastructure improvements.

Governmental entities rarely use power of condemnation to acquire existing structures for general redevelopment, with the exception of dilapidated or nuisance-type properties.

## **2.10 Taxes Applicable to a Transaction Taxes**

A deed presented to a county auditor to begin a transfer process must include a Conveyance Fee Statement signed by the buyer that indicates the purchase price. The county auditor then collects a transfer tax of USD1 per USD1,000 of the purchase price, payable to the State of Ohio. Counties may choose to charge additional transfer tax, up to USD4 per USD1,000 of the purchase price.

By statute, sellers are obligated to pay transfer taxes. In rare cases, parties may negotiate for buyers to pay. Certain transactions are exempt from the taxes, such as transfers without consideration and transfers to or from a governmental entity.

### **Transactions not Involving Transfer by Deed**

In transactions not involving transfers by deed – eg, sales of shares in companies – transfer taxes don't apply. The Ohio legislature is currently evaluating whether to tax indirect transfers.

### **Other Costs**

Besides transfer taxes, the largest costs in real estate transfers are typically brokerage commissions and title insurance survey costs. A seller listing property through a broker is generally expected to pay the brokerage fee; a broker representing a buyer will normally take a share of the fee payable to the seller's broker. Title insurance costs are established by the Ohio Department of Insurance and aren't subject to negotiation. Rates vary depending on coverage amounts.

Responsibility for title cost payment is a matter of local custom. In southwestern Ohio (eg, Cincinnati and Dayton), buyers typically pay title costs, while in central Ohio (Columbus and environs) the sellers typically pay, and in northern Ohio (especially Cleveland), parties often split the costs. The buyers and sellers can also negotiate the costs.

If a seller is dividing property from a larger parcel or has a deficient legal description, it's often asked to provide a survey. In most other circumstances, the buyer will determine whether to obtain a survey and will pay the cost.

### **2.11 Rules and Regulations Applicable to Foreign Investors**

Ohio requires registration of real property acquired by non-resident aliens (those not citizens of and not living in the USA), which applies if a property exceeds three acres or has value exceeding USD100,000 (or USD50,000 in the case of mineral interests). The requirement also applies when a corporation or other business entity acquires property in which a non-resident alien holds at least a 10% interest, or in which a combination of non-resident aliens acquires at least a 40% interest. The registration must be made with the Ohio secretary of state within 30 days of acquisition.



## 3. REAL ESTATE FINANCE

### 3.1 Financing Acquisitions of Commercial Real Estate

In Ohio mortgage loans are the most common form of commercial real estate acquisition financing. They secure debt via a mortgage encumbering the real estate being purchased. Buyers may also obtain mezzanine financing, where debt is typically secured by a pledge of the acquiring company's ownership interests, or other equity arrangements. A variety of financial service and insurance companies provide both mortgage and mezzanine loan financing.

### 3.2 Typical Security Created by Commercial Investors

Mortgage lenders usually procure first-lien mortgages on applicable real estate and take security interest in the fixtures, personal property, leases and other rights (such as mineral rights). Additionally, lenders typically require separate assignments of leases and rents and Uniform Commercial Code (UCC) financing statements for fixtures and personal property. Mortgages and assignment of rents should be recorded in the counties in which properties are located.

UCC fixture financing statements should be recorded with county recorders, but mortgages may serve as fixture filings if they include certain language. UCC financing statements for personal property should be filed with the secretary of state of the state in which the borrower is organized.

### 3.3 Regulations or Requirements Affecting Foreign Lenders

Ohio Revised Code Section 5301.254 requires non-resident aliens to file an Ohio Non-Resident Alien Land Registration form under certain circumstances. Additionally, non-US lenders should review laws and regulations and seek

guidance on the business and tax consequences of operating in Ohio.

### 3.4 Taxes or Fees Relating to the Granting of Enforcement of Security

No mortgage recording tax is payable upon recordation of the mortgage in Ohio, but a filing fee is required.

### 3.5 Legal Requirements before an Entity Can Give Valid Security

In mortgage transactions, borrowers must comply with requirements in governing documents relating to transaction authorizations and loan document executions.

### 3.6 Formalities When a Borrower Is in Default

In Ohio, a judicial foreclosure state, a remedy involving a property sale requires a foreclosure action, service of the complaint in accordance with Ohio Civil Rules and a foreclosure decree entered by the court following any required discovery and litigation. Pre-suit title research by a licensed title insurer is also required.

Loan terms may create pre-conditions to filing. For example, if a pre-condition to exercising remedies under a mortgage is the existence of a default under the loan – and the loan requires a written notice and opportunity to cure – the courts will treat these conditions as prerequisites to filing a foreclosure action.

Effective upon the filing of a foreclosure action, no future liens may attach. The lender's priority regarding liens attached prior to the foreclosure action is dictated by the time of the lien's county recordation.

### 3.7 Subordinating Existing Debt to Newly Created Debt

Debt holders can enter into agreements to subordinate existing secured debts to newly created

debts. These agreements are typically recorded in the county where the real estate is located.

### **3.8 Lender's Liability under Environmental Laws**

If a lender becomes an owner or operator of contaminated property through lien enforcement, it may seek protection under Ohio's secured creditor exemption, which mirrors the federal Comprehensive Environmental Response, Compensation and Liability Act (CERCLA). It's unlikely that the exemption will apply to creditors who participate in operations management, including arranging for the disposal or transport of hazardous substances. Accordingly, lenders should avoid any role in managing treatment or disposal operations concerning the secured property.

### **3.9 Effects of Borrower Becoming Insolvent**

Outside of bankruptcy, Ohio follows the Uniform Fraudulent Transfer Act (UFTA), under which an obligation or lien created to hinder other creditors may be avoided. Similarly, the lien may be avoided if it's granted without an exchange of reasonably equivalent value when the borrower is insolvent.

### **3.10 Taxes on Mezzanine Loans**

There are no existing regulations in relation to mezzanine loans.

## **4. PLANNING AND ZONING**

### **4.1 Legislative and Governmental Controls Applicable to Design, Appearance and Method of Construction**

Typically, new construction or structure renovations first require support from a municipal planning commission, followed by final approval from a zoning board or the municipality's legislative body, the city council. If the property's planned

use changes significantly, or if a non-conforming use that would be altered by the construction or renovation was previously permitted, the new plans must be approved by the zoning board and/or city council.

### **4.2 Regulatory Authorities**

Regulations for development are usually reflected in municipal charters, master plans and zoning codes. Typically, cities designate districts permitting industrial, commercial or residential buildings, along with various activities and plans for uses like parks or waterfront developments.

### **4.3 Obtaining Entitlements to Develop a New Project**

Developers or owners usually submit requests to cities for new development projects and then provide details at planning commission and/or board of zoning appeals hearings. After public hearings that allow opportunity for public comment, plans must be approved by planning and zoning bodies and/or city councils, which issue building and occupancy permits.

### **4.4 Right of Appeal against an Authority's Decision**

Once zoning boards or city councils take final action, parties denied approval can appeal to common pleas courts. Most challenges assert that the denial was arbitrary or contrary to the state's constitution.

### **4.5 Agreements with Local or Governmental Authorities**

Most zoning codes do not require developers and governmental agencies to enter into separate written agreements to obtain planning approvals or building permits, except in planned unit development districts. In many cases, however, developers, governmental agencies and school districts enter into development agreements in connection with awarded governmental incentives, such as:

- tax abatement or tax increment financings;
- public utilities or improvements required to support projects;
- limitations placed due to approval of conditional uses; or
- local hiring or prevailing wage requirements.

## 4.6 Enforcement of Restrictions on Development and Designated Use

Regulations in zoning codes specify the manner and location permitted for different development types. Restrictions enforcement may take many forms, such as denial of building or occupancy permits, citations from building inspectors for violations of existing regulations, or court actions to enjoin activities or compel corrective actions.

## 5. INVESTMENT VEHICLES

### 5.1 Types of Entities Available to Investors to Hold Real Estate Assets

Ohio real estate assets may be held by corporations, limited liability companies (LLCs), limited partnerships (LPs) or general partnerships (GPs). Each entity form is governed by a separate chapter of the Ohio Revised Code: corporations (1701), LLCs (1705), LPs (1782) and GPs (1776).

### 5.2 Main Features of the Constitution of Each Type of Entity

Each of the four principal entity types has unique advantages and disadvantages.

#### Limited Liability Companies

Currently, LLCs are the most common entities utilized to hold title to real estate. An LLC provides limited liability to its owners (“members”), continuity of life, flexibility of allocation of profits and management rights, and the ability to be taxed as a partnership and pass tax attributes to members.

#### Limited Partnerships

LPs provide a set of structural options similar to LLCs, with one significant difference: the general partner bears unlimited personal liability for the LP’s obligations and debts.

#### General Partnerships

Historically GPs often were used to hold real estate because they were easy to establish (no initial written agreement is required, although it’s highly recommended). Owners, however, have unlimited liability for business debts and judgments. All partners share equally in the rights and responsibilities of managing the business, and each partner is responsible for the others’ actions.

#### Corporations

Corporations can be used to acquire real estate assets. It’s essential owners comply with ongoing formalities to retain this entity form’s advantages, including shareholder limited liability for debts and judgments. Corporations are able to raise capital through stock sales, and owners risk only their investments.

Corporation profits, however, may be taxed twice (at the corporate level and on distributions) because corporations are treated as separate entities with no ability to pass tax attributes to shareholders.

### 5.3 Tax Benefits and Costs

In general, LLCs, LPs and GPs present the opportunity for pass-through of tax attributes of property ownership and they avoid the potential for double-level taxation associated with corporate ownership. A corporation may elect to be taxed as a REIT under the Internal Revenue Code to achieve special tax advantages (see **8. Tax** for more general discussion of Ohio-specific tax-related items).

## 5.4 Applicable Governance Requirements

### Corporations

Those creating corporations must prepare and file articles of incorporation with the Ohio secretary of state and provide the authorized number of shares and their par value, as well as identify an Ohio-registered agent for service of process. They must prepare codes of regulations (bylaws) outlining governance, including meeting and voting rights, for both the board of directors and shareholders.

### Limited Liability Companies

Those forming LLCs must file articles of organization with the Ohio secretary of state. An operating agreement provides the various governance provisions, including management rights, rights to distributions and any special voting rights.

### Limited Partnerships

An LP formation requires documentation similar to that for an LLC, with a certificate of limited partnership filed with the Ohio secretary of state. An LP agreement can address various rights and obligations, but limited partners aren't permitted to participate in management or they risk losing liability protection.

### General Partnerships

GP formation requires no written action or government filings. Unless provided otherwise in a written partnership agreement, each partner is entitled to an equal say in management and voting.

## 6. COMMERCIAL LEASES

### 6.1 Types of Arrangements Allowing the Use of Real Estate for a Limited Period of Time

Land may be utilized under lease, license or easement.

#### Lease

A lease is a conveyance of a landlord's present possessory interest in property for a term of less than the landlord's own term of ownership. Under Ohio law, a lease must contain all material terms of the agreement (ie, consideration, term, premises description). A lease may be written or oral, but, to avoid defenses under Ohio's statute of frauds and statute of conveyances, a lease of more than one year must be in writing, and a lease of greater than three years must be both acknowledged by the landlord and the tenant before a notary public and recorded in public land records. In lieu of a recording of the entire lease, Ohio allows for the recording of a memorandum of lease, but the constructive notice is limited to the matters contained in it.

#### License

A license is a personal right (typically revocable and non-assignable) to use or perform some action on another's property. Either written or oral, it's generally terminable at the licensor's will, subject to the terms of the license agreement.

#### Easement

An easement is a right to use another's property for a definite or indefinite timeframe. Easements are generally created by written agreement, but Ohio courts have recognized other means of creation:

- by prescription, where the easement has been non-permissively used in an open,

- continuous and adverse manner for at least 21 years;
- by implication, where a conveyance of property includes whatever is necessary for its beneficial use and enjoyment;
- by necessity; and
- occasionally by estoppel.

## 6.2 Types of Commercial Leases

All commercial leases are generally subject to the same legal framework and enforcement, but the typical structure and terms of commercial leases will depend on the usage type, such as office, retail, industrial or special use.

Lease transactions often involve negotiations over issues like maintenance and repair obligations, alterations, assignment and subletting, indemnities, law compliance, hazardous waste, casualty, insurance, renewal and extension rights, surrender provisions, default and remedies and more.

Leases may be structured as “ground leases,” where tenants lease the land and are responsible for building construction, typically under long-term arrangements. Ground leases generally involve a great deal of planning, negotiation and drafting, including coordination with project lenders to achieve a “financeable” ground lease.

### Office Leases

In office leases of multi-tenant buildings, tenants typically pay fixed-base rents plus proportionate shares of increases in building operating expenses over the base years. These includes real estate taxes, insurance, maintenance and repairs, and other operating expenses, which are passed through to tenants, often on a monthly basis. Tenants can often negotiate rent-free periods and other concessions as inducements to lease building space, including generous tenant build-out allowances.

### Retail Leases

Retail leases will normally set forth a minimum rent plus a percentage rent based on stores’ gross sales. Tenants typically pay shares of common-area maintenance costs in larger facilities. Retail leases contain several unique provisions, including operating covenants, recapture rights, exclusive-use provisions, radius clauses, co-tenancy requirements and shared-parking provisions.

### Industrial Leases

Industrial leases are often done on a “triple net” basis, meaning tenants pay base rents and all building ownership, operations, maintenance and insurance costs.

## 6.3 Regulation of Rents or Lease Terms

Apart from rent limitations that may apply to residential properties developed or financed under government low-income housing programs, Ohio has no rent restrictions for either commercial or residential leases. Lease terms for commercial leases are not regulated by state law. Residential leases are generally covered by the Ohio Landlord-Tenant Act, which establishes the statutory duties of both parties and sets forth mandatory rental agreement terms.

## 6.4 Typical Terms of a Lease

Parties to a commercial lease may negotiate lease terms, which vary depending on asset types and parties’ leverage.

## 6.5 Rent Variation

Parties to commercial leases may structure rent adjustments as they choose. The most common is periodic increases, either annually or at other intervals.

## 6.6 Determination of Changes in Rent

Parties to commercial leases may structure rent changes as they choose. No regulatory framework governs rent increases.

## 6.7 Payment of VAT

Ohio does not collect rent taxes.

The state does impose an annual Commercial Activities Tax (CAT) on the privilege of doing business. It applies to most businesses with taxable yearly gross receipts exceeding USD150,000, regardless of organizational structure. Businesses must register with the state of Ohio at its online portal.

## 6.8 Costs Payable by Tenant at the Start of a Lease

Tenants typically bear a portion of build-out costs to prepare spaces for occupancy and often pay landlords security deposits. Build-out costs vary considerably, but typically tenants negotiate tenant allowances (TI Allowances) whereby landlords fund some improvements. Landlords set security deposits based on tenants' creditworthiness and the measures of performance risk.

## 6.9 Payment for Maintenance and Repair

Tenants typically pay directly or indirectly for common-area costs.

In a "gross lease," rent payable to a landlord is a gross amount and includes the tenant's obligations for common-area charges. The landlord pays the costs and performs the work associated with common areas and recovers the charges through the tenant's rent.

In a "net lease," the rent payable is net to the landlord, and the tenant pays (or reimburses the landlord) for additional charges comprising common-area expenses, typically on a proportionate basis, based on the square footage of the leased premises in relation to the building's total leasable area.

## 6.10 Payment for Services, Utilities and Telecommunications

Utility services are frequently metered separately or sub-metered for each tenant, particularly in newer properties. For properties without separate metering, charges may be included in operating expenses and shared among tenants. Telecommunications are often handled by each tenant.

## 6.11 Insuring Real Estate That Is the Subject of a Lease

Typically, landlords provide insurance on buildings and tenants insure trade fixtures. The costs can be handled as described in **6.9 Payment for Maintenance and Repair**. In a gross lease, the rent includes insurance; in a net lease, the insurance costs are reimbursed or paid by the tenant. In a ground lease, the lessee will typically maintain the casualty insurance.

Most casualty occurrences (such as fire) are covered by basic "all-risk" property insurance policies. Special "riders," often with an additional cost, may be needed to cover events like floods, earthquakes or terrorism.

## 6.12 Restrictions on the Use of Real Estate

Landlords may impose any use restrictions they deem appropriate.

Real estate use is also controlled by local zoning laws. Regulations vary by jurisdiction, but often provide for alternate zoning classifications and permitted use, such as residential, office, mixed-use, industrial, etc. Zoning regulations may also govern density, setback, height, parking and other project features.

## 6.13 Tenant's Ability to Alter or Improve Real Estate

Parties to a commercial lease may structure rights to alter property as they choose. Land-

lords' rights to approve tenants' alteration scopes or designs are one aspect of negotiations. Typically, landlords will impose requirements, including approval of plans and specifications, compliance with law, insurance provisions, indemnity, prohibition on structural alterations, the right to approve contractors and the obligation to remove/restore upon lease expiration.

## 6.14 Specific Regulations

As noted above, local land use regulations govern the use, design and construction of structures or other improvements. State building codes also affect construction in applicable cases. Architects or engineers advise on these requirements and restrictions.

## 6.15 Effect of Tenant's Insolvency

Insolvency is governed largely by the US Bankruptcy Code, which overrides any contract or lease stipulations. Provisions addressing bankruptcies, therefore, are generally unenforceable.

## 6.16 Forms of Security to Protect against Tenant's Failure to Meet Obligations

Security forms are the same as with any commercial payment obligation and include cash security deposits, lease guarantees and letters of credit.

## 6.17 Right to Occupy after Termination or Expiration of Lease

Technically, a tenant does not have a right to continue to occupy real estate after the expiration or termination of a lease. If a landlord acquiesces, however, and doesn't object to the tenant remaining in the leased premises, and/or continues to accept rent, the parties will likely be deemed to have either extended the lease or continued the relationship as a tenancy at will.

Commercial leases typically contain a clause indicating that rent increases upon a holdover,

often at 125% to 200% of the rent previously in effect, and that tenants are responsible for damages arising from the holdover.

Landlords can evict tenants by judicial action upon short notice if tenants remain in possession of the premises following lease-term expiration.

## 6.18 Right to Terminate Lease

Under most commercial leases, landlords may terminate leases for rent non-payment or other material breach-of-lease obligations. Tenants typically receive a short grace period for rent non-payment and a longer period (often 30 days after notice) for other non-performances, such as failure to maintain the property or operate in accordance with lease terms.

## 6.19 Forced Eviction

Tenants can be evicted prior to lease expiration based on defaults. Written leases typically contain the circumstances in which landlords can evict tenants; if a lease doesn't define terms, any material lease breach is valid grounds for eviction.

Landlords with grounds to evict tenants must file court eviction complaints and provide hearing testimony on the lease breaches and necessity of eviction.

Courts usually rule at hearings or soon after. If they find in the landlord's favour, they typically grant tenants time to leave the premises (usually two to 14 days). If tenants don't comply, landlords may ask local sheriffs to intervene.

## 6.20 Termination by Third Party

Governmental and other authorities (like public utilities) may take property by eminent domain (or "condemnation") for broadly defined public purposes. State law outlines procedures for taking ownership of property; they typically include the

termination of all leases encumbering the property. The condemning authority must pay the fair market value of the property being acquired. In the absence of a negotiated agreement between the government and the property owner, courts will conduct a trial to determine fair market value, with each party providing property valuation appraisals and expert witnesses.

The allocation of condemnation proceeds between landlord and tenant is subject to the terms negotiated by the lease parties.

## **7. CONSTRUCTION**

### **7.1 Common Structures Used to Price Construction Projects**

Commonly, construction projects are priced with fixed-cost or “cost plus a fee” structures that often include a guaranteed-maximum price. Typical pricing considerations are project complexity, time constraints, financing requirements and design documents stage of development.

### **7.2 Assigning Responsibility for the Design and Construction of a Project** **Design-Bid-Build**

The owner contracts with a designer to prepare complete design documents, then retains a general contractor (or several trade contractors) to build the project. Design-bid-build projects are typically bid by the owner to multiple contractors to encourage pricing competition. Because the design documents are complete, a fixed-price bid is commonly required.

### **Construction Manager-at-Risk**

The owner retains both a design professional and a construction manager, often through a competitive proposal process, to provide pre-construction services like cost estimating, constructability review of design documents, bid packaging and schedule consulting. At an

agreed-to stage of the design, the designer delivers the interim design documents to the construction manager for pricing. The construction manager becomes the “at-risk” contractor upon the owner’s acceptance of the construction manager’s guaranteed maximum price proposal for the work and, as such, guarantees the price and schedule and holds all the trade contracts, which are usually competitively bid by the construction manager.

### **Design-Build**

The owner develops project criteria in the form of preliminary drawings and performance specifications; these documents may be prepared by the owner’s inhouse design staff or through a third-party design professional. The “criteria documents” are then used to solicit bids from design-build firms to complete the design documents and build the project under a single contract with the owner. The design-build entity may be a sole firm (typically a contractor) that subcontracts the design work, or a separately formed joint venture or limited liability company that includes a contractor and a design firm as joint venturers or members.

### **7.3 Management of Construction Risk** **Indemnification**

Contracts typically include an indemnification from the contractor in favour of the owner covering claims or damages the owner might incur due to contractor negligence. The indemnification is usually coupled with the contractor’s obligation to add the owner as an additional insured to the contractor’s commercial general liability policy for any claims for bodily injury or property damage arising out of the contractor’s work at the project site. Like many states, Ohio has an anti-indemnification statute (ORC Section 2305.31), which prevents an owner from requiring a contractor to indemnify the owner for the owner’s negligence.



## Construction Contracts

Construction contracts typically include general warranties from the contractor stipulating that all items furnished and installed by contractors will be new (unless otherwise specified) and free of defects. They usually contain a clause specifying “duty to correct” defective or incomplete work within one year of substantial completion, unless another timeframe is negotiated.

## Waivers

Clauses that waive or limit overall liability of contractors or design professionals are common in larger contracts and are enforceable if the clause is conspicuous and terms are clear and straightforward. Enforceability is determined on a case-by-case basis, and clauses aren’t enforced if the breaching party was grossly negligent or if the contract is shown to be unconscionable.

Consequential damages are often waived by both parties. While “no damage for delay” clauses are typical, they’re strictly construed and limited by common-law exceptions (eg, fraud or bad faith) and by ORC Section 4113.62, which renders such clauses unenforceable if delays are a proximate result of the owner’s act or failure to act.

## 7.4 Management of Schedule-Related Risk

Liquidated damages are often imposed to assure timely completion of project or key milestone dates. They are enforceable in Ohio if they do not penalize a party.

## 7.5 Additional Forms of Security to Guarantee a Contractor’s Performance

Performance and payment bonds are required on public construction projects (ie, where the owner is a public government agency) with few exceptions, but they’re not normally required by private-party owners on construction projects. Occasionally, a private-party owner will require

a letter of credit for some portion of the contract price (20–40%) in lieu of the bond. Most private-party owners, however, forgo bonds or other financial security instruments to save costs, especially where the contractor has a proven track record of successful job performance and demonstrates that it has sufficient financial strength to sustain a major subcontractor default.

## 7.6 Liens or Encumbrances in the Event of Non-payment

In the event of non-payment, contractors, subcontractors, material suppliers, labourers and, in limited circumstances, design professionals have the right to place a “mechanic’s lien” on property that the lien claimant worked on or supplied materials for. Ohio’s mechanic’s lien law (Revised Code Chapter 1311) specifies the various notice, timing and filing requirements for the preservation and perfection of a mechanic’s lien.

Generally, mechanic’s liens are effective the date of a statutory notice of commencement (NOC) recording or, in the absence of such recording, the date of first visible work or furnishing of materials at the project site. Lien claimants have priority over a mortgage filed after the effective date of the mechanic’s lien, regardless of when the labour or furnishing began.

A mortgage that qualifies as a “construction mortgage loan” under ORC Section 1311.14, however, has priority over any mechanic’s liens, even if the mortgage is filed after the NOC is recorded or the construction commenced. The statute details the requirements that must be satisfied to obtain this “super-priority”; for example, the construction mortgage must contain certain information, it must be used to finance improvements or pay off prior encumbrances, and the proceeds of the construction loan must be distributed in the manner dictated in the statute.

## 7.7 Requirements before Use or Inhabitation

A “certificate of occupancy” is typically required. This document certifies compliance with the Ohio Building Code and other applicable local building codes and will outline the legal use of the property, the occupant load and any special conditions relating to the property use.

## 8. TAX

### 8.1 Sale or Purchase of Corporate Real Estate

In Ohio, real estate transfers are subject to a “conveyance fee” or “transfer tax,” composed of a state component (at USD1 per USD1,000) and a county component (up to USD3 per USD1,000).

A variety of exemptions are available, including certain related-party transfers involving no consideration. See **2.10 Taxes Applicable to a Transaction**.

By Ohio statute, the seller/grantor is obliged to pay the tax, but it’s subject to negotiation in each particular transaction.

### 8.2 Mitigation of Tax Liability

To avoid conveyance fee taxes, a transfer of entity interests may be used, if properly structured. The Ohio legislature is currently considering proposals to address this issue, so indirect transfers may be taxed in the future.

### 8.3 Municipal Taxes

In Ohio, there is no tax on rents or occupancy.

### 8.4 Income Tax Withholding for Foreign Investors

**Income Tax Withholding for Foreign Investors**  
Individual investors who aren’t US residents (ie, who are not US citizens, don’t hold a “green

card” or do not spend substantial time in the USA) and who have US-source income effectively connected with a US trade or business, are subject to US federal income tax at graduated tax rates up to 37%. Assuming an IRS Form 1040NR is timely filed, deductions are permitted to reduce US-source gross income. Foreign investors who realize US-source investment income (fixed, determinable, annual or periodical [FDAP] income such as interest, dividends and rents) are subject to a 30% withholding rate on such FDAP income, which may be reduced based upon tax treaty provisions, provided the foreign investor furnishes required information to the payor on the IRS Form W-8 series.

The rules for non-US corporations are similar in that these overseas corporations are subject to a flat 21% tax rate on US-source income, either effectively connected with a US trade or business or attributable to a permanent establishment in the United States. Assuming an IRS Form 1120F is timely filed, deductions are permitted to reduce US-source gross income.

Likewise, non-US corporations are subject to 30% withholding on FDAP (subject to treaty reduction). Certain foreign corporations may also be subject to 30% withholding under the Foreign Account Tax Compliance Act if they haven’t registered or furnished required information to the IRS or the their home country investor’s governmental taxing authority. Finally, non-US corporations are subject to a 30% branch profit tax for earnings remitted (or deemed remitted) outside the USA. The tax rate may be reduced pursuant to an applicable tax treaty.

Non-US investors and corporations receiving income allocations passed through from US partnerships, or selling US partnership interests, are subject to US withholding tax and information reporting.

## Ways to Reduce or Alleviate Such Taxes

Withholding taxes may be reduced based upon the terms of applicable tax treaties between the USA and the foreign governmental taxing authority. Tax treaties generally don't provide relief for taxes imposed under the Foreign Investment in Real Property Tax Act (FIRPTA) regime (discussed below).

## How Gains from the Disposition of Real Property Are Taxed and how Foreign Investors Are Taxed Differently

Pursuant to FIRPTA, gains from the sale of US real property interests are treated as generating "effectively connected" US-source income and may be taxed to foreign investors at a 20% capital gains tax rate (or at graduated rates up to 37%) or to foreign corporations at a 21% tax rate. A foreign corporation is also subject to the branch profits tax described above. The buyer generally must withhold 15% of the purchase price to cover tax liability. The non-US investor or corporation should file a US tax return (IRS Form 1040NR for individuals and IRS Form 1120F for corporations) to report the gain or loss and related tax liability; the 15% withholding is treated as a payment on the tax liability. A foreign investor may have to pay additional US income tax or may be entitled to a refund of part or all of the withholding tax. In addition, the FIRPTA rules can apply to the sale of stock of a domestic corporation that holds substantial real estate.

## Exemptions

FIRPTA offers some exemptions; eg, sales of publicly traded stock may be exempt in certain cases.

## 8.5 Tax Benefits

Non-residential real estate is depreciated on a straight-line basis over 39 years, and residential real estate used in a rental activity is depreciated on a straight-line basis over 27.5 years. Certain property is depreciated over 15 years. In some

situations, an affirmative election may have to be made to deduct expenses.

US entities may leverage real estate on a tax-deferred basis, but distributions to foreign investors or foreign corporations may be subject to tax under certain circumstances. Recent changes to US tax law have largely eliminated certain tax deferral strategies, including those featuring a so-called bottom-dollar guarantee.

## 8.6 Key Changes in Federal Tax Reform

The Tax Cuts and Jobs Act (TCJA) enacted a 20% deduction from taxable income for qualified business income generated by pass-through entities such as partnerships, S-corporations and LLCs. The deduction is subject to a limitation based on wages paid by the pass-through entity and/or on a percentage of the unadjusted basis of tangible property used in the business of the pass-through entity. The deduction also applies to ordinary dividends from REITs.

The TCJA placed a limit on interest deductions, which are now restricted to 30% of the sum of business interest income and EBITDA (earnings before interest, taxes, depreciation and amortization) (2018–2021) or EBIT (earnings before interest and taxes) (post-2021). An election out is permitted for any real property trade or business provided the business extends the depreciation term for its real estate assets.

The TCJA limits tax-deferred like-kind exchanges to real property only.

Transfers of 50% or more of the capital and profits interest of a partnership within a 12-month period will no longer cause a technical tax termination of the partnership. Previously, such a technical tax termination closed the partnership's tax year, cancelled existing tax elections and caused depreciable lives to be reset.

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**Thompson Hine LLP** provides clients with a real estate team of 43 primary and secondary members located across all offices: Atlanta, Cincinnati, Cleveland, Columbus, Dayton, New York, and Washington, DC. The team's main practice areas comprise corporate real estate, including headquarters projects and plant facilities; real estate construction and development; asset management and leasing; financing, investment and capital markets transactions; and tax credits and other government incentives. Drawing from the collective experience

of Project Management Consultants, the firm's wholly owned subsidiary, and practice groups such as construction, bankruptcy, tax, corporate, environmental and business litigation, the real estate team offers sophisticated counsel on property transactions of every size and complexity. It also guides clients in litigation and settlement strategies, foreclosures, workouts, bankruptcies affecting other real estate investments, brownfields, eminent domain and land-use matters.

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