



BANKRUPTCY v. RECEIVERSHIP v. ASSIGNMENT FOR THE BENEFIT OF CREDITORS

Advantages and Disadvantages of Each

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BANKRUPTCY	RECEIVERSHIP	“ABC”
<i>Commencement of Proceeding; Who Manages the Debtor?</i>		
<p><u>Chapter 11</u></p> <p>Voluntary Petition filed by Debtor.</p> <p>Management remains in place unless extraordinary remedy of appointment of Chapter 11 Trustee</p> <p><u>Chapter 7</u></p> <p>Voluntary Petition filed by Debtor; involuntary petition filed by 3 creditors holding unsecured claims totaling more than \$12,300; or conversion from Chapter 11.</p>	<p>Complaint filed by secured creditor. Typically filed in connection with foreclosure action, though not required.</p> <p>Most deeds of trust contain debtor’s consent to <i>ex parte</i> appointment of receiver. If so, court will typically enter order without notice. Absent such a provision, order appointing receiver typically entered only after notice to debtor and opportunity to object. Standard for appointment, absent contractual consent, is typically comparable to grounds for</p>	<p>The Assignee takes control of all of the Debtor’s assets once the assignment has been made and accepted. Management of the Debtor, including the Board of Directors, loses the ability to control decision making over the affairs of the Debtor once the assignment has been accepted by the Assignee.</p> <p>The Assignee is a fiduciary who acts in the best interests of creditors of the estate, namely to take possession of the assets, maximize the recovery from the assets and then to distribute the proceeds of the liquidation to creditors pursuant to the priorities established under</p>



<p>Chapter 7 Trustee randomly appointed from pool of panel trustees; though creditors have the ability to elect a trustee.</p> <p><u>Fiduciary Duties</u></p> <p>DIP or Trustee is fiduciary to creditors and estate.</p>	<p>entry of preliminary injunction.</p> <p>Creditor seeking appointment typically selects receiver with appropriate skills for project. Courts generally defer to creditor's selection of person or entity to serve as receiver, but are not required to.</p> <p><u>Fiduciary Duties</u></p> <p>Receiver is officer of court, and must be careful to act in the interests of the estate, and not just the interests of the creditor seeking receiver's appointment.</p>	<p>state law.</p>
<p><i>Assets of Estate</i></p>		
<p>All debtor's assets.</p>	<p>Assets that are the subject of the secured creditor's claim.</p> <p>Creditor should be careful to limit scope of receiver's authority to assets in receivership that are collateral for loan; not all assets of debtor, nor debtor itself. If debtor is not SPE, even more important to clarify those assets that are the subject of the receivership proceeding.</p>	<p>All of the debtor's assets.</p>



<i>Management Authority</i>		
<p><u>Chapter 11</u></p> <p>Debtor is “debtor-in-possession” with authority to operate company in ordinary course of business.</p> <p>Debtor is prohibited from paying pre-petition debts without court approval.</p> <p>Debtor may not borrow funds on secured basis without court approval.</p> <p>Debtor may not sell assets outside ordinary course of business without court approval.</p> <p>Debtor may not retain or compensate professionals without court approval.</p> <p><u>Chapter 7</u></p> <p>Typically does not contemplate operating business, though Chapter 7 trustee may seek interim authority to operate business if going concern sale is feasible.</p>	<p>Authority of receiver is defined in Order Appointing Receiver.</p> <p>Creditor seeking appointment has significant discretion in vesting receiver with authority to continue business operations without additional Court approval. Typical Order Appointing Receiver authorizes receiver to:</p> <ul style="list-style-type: none"> • Operate business in ordinary course • If subject of receivership is development project, order may authorize receiver to complete pending construction and/or to sell completed units/lots/houses in ordinary course without further Court approval • Pay pre-petition claims if in best interest of Receivership estate • Borrow funds (typically from creditor seeking appointment) secured by Receiver’s certificates and first lien on 	<p>Management authority over the assigned assets vests with the Assignee. The duties of the Assignee are typically defined in the assignment contract and applicable provisions of state law.</p> <p>The Assignee will generally not operate the business of the debtor unless there is reasonable assurance that the operations will generate more value from the assets than the costs to operate during that period.</p>



	<p>debtor's assets</p> <ul style="list-style-type: none"> • Retain and compensate employees and professionals needed to assist receiver in performing duties • Sale of assets outside ordinary course of business is usually conditioned on entry of separate court order <p>If development project includes HOA, Order Appointing Receiver should clarify that receiver is entitled to appoint debtor representatives to HOA board.</p> <p>If debtor owns more than one project, and only one project is subject of receivership, Order Appointing Receiver should address receiver's ability to use and compensate common administrative personnel, access to books and records in corporate HQ, other similar concerns.</p>	
<i>Compensation of Management</i>		
<p><u>Chapter 11</u>. Management is paid in ordinary course of business. In rare cases, compensation paid to management may be challenged by creditors as excessive.</p>	<p>Order Appointing Receiver defines compensation of receiver. Most common compensation structures:</p>	<p>The general assignment agreement will include as one of its terms the amount of compensation to be paid to the Assignee as well as the ability of the Assignee to be</p>

<p>Bankruptcy Code imposes limits on retention bonuses.</p> <p>Chapter 11 Trustee is paid percentage of funds distributed to creditors (though confirmed Chapter 11 plan may compensate a plan trustee in a different fashion).</p> <p><u>Chapter 7.</u> Chapter 7 Trustee is paid percentage of funds distributed to creditors.</p>	<ul style="list-style-type: none"> • Hourly rate • Flat monthly fee • Percentage of funds distributed to secured creditor 	<p>reimbursed for its out-of-pocket expenses, and the ability to hire professionals (lawyers, accountants, etc.). Compensation can be on a percentage of dollar value generated from the liquidation of the assets; on a flat fee basis; and in some instances Assignees charge on an hourly rate basis for time spent administering the estate.</p>
<p><i>Automatic Stay</i></p>		
<p>Statutory automatic stay against creditors' seeking to collect pre-petition claims against estate.</p> <p>In single asset real estate cases –[debtor owns real property constituting a single property or project which generates substantially all of the gross income of a debtor, and on which no substantial business is conducted by the debtor other than operation of the real property, excluding family farms and residential real property with fewer than 4 residential units] - stay automatically expires after 90 days (which may be extended by court order), unless</p> <ul style="list-style-type: none"> • Debtor has proposed plan of reorganization that has reasonable possibility of being confirmed within reasonable time; or • Debtor has commenced monthly 	<p>No statutory automatic stay.</p> <p>Order Appointing Receiver generally stays parties to receivership proceeding, and parties with notice or actual knowledge of entry of order, from interfering with operation of receivership estate.</p> <p>Further relief is typically secured through</p> <ul style="list-style-type: none"> • Separate injunction action; or • Order to present and file claims, which may allow participation in distribution from estate only upon consensual stay of any other litigation 	<p>State law(s) will not have an automatic (that is solely a bankruptcy provision and therefore limited to bankruptcy cases.) State law however provides that an assignee will have a perfected lien on assets as of the date of the general assignment (<i>see</i> Uniform Commercial Code §9-309), junior to any existing secured claims. This lien effectively limits unsecured creditor's ability to enforce a judgment (or pre-judgment writ) obtained after the making of the assignment as it will be junior to the lien right of the assignee.</p> <p>Senior secured creditors' rights are not affected by the assignee's lien rights. Such senior secured creditors retain their right to their collateral. The assignee must obtain the senior secured creditors' consent to liquidate</p>

<p>payments to each secured creditor in an amount equal to the nondefault contract interest on “the value of the creditor’s interest in the real estate.”</p> <p>Miscellaneous other exceptions to automatic stay.</p>		<p>the secured creditor’s collateral or tender possession to the secured creditor.</p>
<p><i>Leases and Executory Contracts</i></p>		
<p>DIP or Trustee may reject leases or executory contracts that are burdensome to estate, upon court approval.</p> <p>DIP or Trustee may assume and assign leases or executory contracts upon court approval, subject to cure of monetary defaults.</p>	<p>Order Appointing Receiver typically provides that receiver may reject leases or executory contracts that are burdensome to estate, upon court approval.</p> <p>Receiver may assume and assign leases or executory contracts upon court approval, subject to cure of monetary defaults. Courts will generally enforce provisions of leases or executory contracts requiring consent of other party to assignment.</p> <p>Most leases and executory contracts contain language to the effect that appointment of a receiver is an event of default.</p>	<p>Most leases and executory contracts contain language to the effect that the making of a general assignment for the benefit of creditors is an event of default. Rarely does an assignee assume and assign a lease unless the lessor has given prior consent.</p>
<p><i>Sales Free and Clear of Liens</i></p>		

<p>Statutory authority for sale of assets free and clear of all liens, claims, and encumbrances, with liens attaching to sales proceeds; if</p> <ul style="list-style-type: none"> • Secured creditor consents to sale; • Sales price is sufficient to satisfy all liens; • Applicable non-bankruptcy law permits such sale; • Liens are in bona fide dispute; • Secured creditor could be compelled, in a legal or equitable proceeding, to accept a money satisfaction of such interest. <p>Some courts limit DIP’s ability to sell all or substantially all of estate assets outside a plan confirmation process.</p> <p>Typically, sales free and clear of liens come with limited representations from DIP or Trustee; buyer relies on Court order for good title.</p> <p>Title insurance companies generally recognize court’s authority to order sales free and clear, and will insure title in purchaser, regardless of affirmative lien release by secured creditors.</p>	<p>Frequently, receiver is “care-taker” pending completion of foreclosure by secured creditor, and thus does not seek to sell receivership assets.</p> <p>In some cases, secured creditor prefers receiver to sell receivership assets, rather than taking ownership itself through foreclosure sale:</p> <ul style="list-style-type: none"> • Collateral is operating business, such as restaurant, and going concern sale maximizes value • Construction defect concerns • Environmental liability concerns • Receiver’s ability to maximize value, rather than more traditional distressed sale by secured lender <p>Courts will typically authorize sale free and clear of liens, with liens attaching to sales proceeds, upon notice to all creditors claiming secured interest.</p> <p>Typically, sales free and clear of liens come with limited representations from Receiver; buyer relies on Court order for good title.</p>	<p>There is no authority under most state laws for the sale of assets free and clear of secured creditor liens. In states with court supervision of assignments, there may be instances where such a court order can be obtained. However, a secured creditor who realizes sufficient value from its collateral will usually consent to the release of its lien as part of the negotiations over the sale price to be obtained for the assets.</p> <p>Where the assignee has sold the assets through an Asset Purchase Agreement, the sale will be on an “as is – where is” basis, without representation or warranty, other than the seller (the assignee) has the authority to enter into the sale and to deliver the acquired assets.</p>
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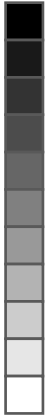


	<p>When other secured creditors are not otherwise parties to receivership proceeding, due process concerns may arise, and it may be necessary to join all secured creditors to proceeding.</p> <p>Title insurance issues may arise if secured creditors refuse to release liens, notwithstanding scope of sale order; particular concern with tax liens.</p>	
<i>Avoiding Powers</i>		
<p>Statutory provisions to avoid preferential transfers, fraudulent transfers, unauthorized post-petition transfers.</p> <p>In addition, traditional avoidance powers under state or common law, including UFTA.</p>	<p>Traditional avoidance powers under state or common law, including UFTA.</p>	<p>18 states have some form of statutory basis for the recovery of a preferential transfer, separate from the ability to recover under the Uniform Fraudulent Transfer Act.</p>
<i>Discharge; Termination of Proceeding</i>		
<p>Chapter 11 debtor can secure discharge through confirmation of plan which preserves going concern business. No discharge for liquidating Chapter 11 debtor or debtor in Chapter 7.</p>	<p>No discharge for debtor.</p> <p>Order approving receiver's final report discharges receiver from further liability.</p>	<p>No discharge of debt is provided for, though the corporate entity has no assets in the remainder or shell.</p> <p>In states where there is court supervision, the</p>



		assignee will seek authority from the court to distribute any remaining funds in the estate and thereafter close the estate; otherwise, final distribution and closure is a decision solely within the discretion of the assignee.
<i>Miscellaneous</i>		
Code gives priority status to numerous pre-petition unsecured claims (unpaid wages, taxes, claims for goods and services provided within 20 days of petition), though priority claims still fall behind secured creditors' claims.	Priority of claims is a function of state law. Claims of any agency of the federal government have priority over all unsecured claims (priority wages, taxes or general unsecured claims) by statute – 37 U.S.C. §3713. Failure to honor this priority carries personally liability to the assignee.	Priority of claims is a function of state law. Claims of any agency of the federal government have priority over all unsecured claims (priority wages, taxes or general unsecured claims) by statute – 37 U.S.C. §3713. Failure to honor this priority carries personally liability to the assignee.
Code authorizes estate to surcharge secured creditor for cost of preserving its collateral.	No statutory surcharge, but creditor seeking appointment of receiver will generally be responsible for shortfall if receiver is unable to pay all expenses of receivership estate.	No statutory surcharge.
	If debtor files bankruptcy after receiver is appointed, Bankruptcy Code contemplates procedure for excusing receiver from turning over receivership estate to DIP, and/or granting administrative priority status	Filing of a bankruptcy proceeding more than 120 days after the making of the assignment results in automatic excusal of turnover of property of the estate by assignee to debtor in possession, unless turnover is necessary to prevent fraud or injustice. In addition, a

	to claims incurred during receivership proceeding.	bankruptcy filing more than 120 days after the date of the assignment is subject to a motion for the court to abstain from taking jurisdiction (and state law plans are generally favored over bankruptcy cases)
Panel trustees have standing bonds for all cases. Chapter 11 trustees and plan trustees may be required to post additional bond, which will be expense of estate.	Receiver must post bond in amount determined by court, which is paid for by receivership estate.	Bond requirements are on a state by state basis.
UST quarterly fees are added expense of administration. Creditors' committees may retain counsel at estate expense, adding to expense of administration.		
DIP must file monthly operating reports.	Receiver files reports as required by Order Appointing Receiver	The assignee must give notice of the assignment and give creditors time to file claims; regular reporting may be required by statute.
	Many SPE's have not secured separate tax ID numbers and use tax ID of parent company. Receiver should be authorized to require parent company to secure tax ID for entity in receivership, or to secure tax ID itself, for banking and tax reporting purposes.	The general assignment contract will usually include a power of attorney to enable the assignee to take actions as necessary on behalf of the company.



Recordation of the general assignment is a function of state law, unless owned real property is included in the assignment, which would require the assignor to provide (typically) a quit claim deed in favor of the assignee.

Order Appointing Receiver should be recorded in real property records, to give all interested parties notice of appointment.

