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The Importance of Ancillary Receivers

By Michael R. Johnson and Austin C. Nate

The Practitioner's Corner is a regular feature where NAFER members can contribute their personal perspective on issues facing receivers.

Commercial receivers and receiverships have become common in today's legal ecosystem. Whether in federal or state court, receivers are regularly appointed to assume or take control over real or personal property assets to maintain the viability of a struggling business or simply to ensure payment to creditors. Unlike regulatory receiverships, which are initiated by federal and state regulatory agencies to remedy suspected fraud or misconduct, a commercial receivership is usually initiated by a creditor to preserve and liquidate collateral after a debtor defaults. The creditor typically wants to gain control of the property to prevent waste or deterioration and to preserve and monetize its investment.

But what happens when the commercial receiver has assets in another state that he or she needs to administer?

How does the receiver obtain control over those assets? One option is to file the receivership action in federal court and take advantage of federal statutory provisions which expressly address the question. But this approach comes with jurisdictional and other limits – as discussed in more detail below. And federal statutory provisions are no help at all when the receivership action has been filed in state court.

With respect to state court receiverships, one of the most effective options, at least in some states and for certain assets, is to look to the Uniform Commercial Real Estate Receivership Act (the "UCRERA"). UCRERA allows a receiver appointed in another state to become an "ancillary receiver" for commercial property located in the appointing court's state. UCRERA is an important tool for state-court receivers whose work involves multiple jurisdictions and who attempt, often on behalf of secured creditors, to deal with

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property in several different states all owned by a single entity.

Until UCRERA was drafted, the state rules governing out-of-state asset administration by a receiver were fragmented and inconsistent. Recognizing the dearth in statutory guidance and the resulting uncertainty surrounding receivership procedure, the National Conference of Commissioners on Uniform State Laws (the "Conference") drafted and in 2015 adopted, the UCRERA to provide uniformity in receivership procedures between states.[1] At the time the Conference adopted the UCRERA, only two states had comprehensive statutory schemes governing the power and appointment of receiverships and related procedures.[2] Since 2015, however, eleven states have adopted the UCRERA, and one more state has introduced legislation to adopt it.[3] These newly-passed laws provide much clarity to the procedures governing receiverships and establish a framework for receivers to fulfill their duties with greater certainty.

UCRERA States

In general, UCRERA applies to any receivership involving an interest in real property and any personal property related to or used in operating the real property, provided the property is used or intended to be used for agricultural, commercial, industrial or mineral-extraction purposes. Since its adoption seven years ago, Arizona, Connecticut, Florida, Maryland, Michigan, Nevada, North Carolina, Oregon, Tennessee, Utah, and West Virginia have enacted UCRERA. Rhode Island introduced legislation to adopt it this year.[4]

Some of the key benefits of the statute include: 1) an automatic stay; 2) authority to sell property free and clear (similar to Section 363 of the Bankruptcy Code); and 3) the ability to incur debt outside the ordinary course with court approval.[5] And importantly, UCRERA also allows a court to appoint a receiver who has already been appointed in another state as an ancillary receiver with respect to real and personal property related to or used in operating the real property, which is located in the appointing court's state.[6] Specifically, the statute allows a court to appoint a receiver appointed in another state "as an ancillary receiver" for property located in the current state as long as the receiver satisfies certain eligibility requirements, A receiver must submit a statement that he or she is not an affiliate of a party or have an adverse material interest to a party or have a material financial interest in the outcome of the action or have a debtor-creditor relationship with a party, and must not hold an equity interest in a party other than a noncontrolling interest in a publicly-traded company (collectively, the "Disqualifying Factors").[7] UCRERA defines "property" to include both real and personal property.[8] Once the foregoing requirements are met, a court may issue its own order giving effect to another order appointing a receiver in a different state, and granting the ancillary receiver all the rights, powers, and duties afforded under UCRERA.[9]

A simple example demonstrates how the UCRERA's provisions resolve the jurisdictional issues resulting from receivership property spanning several states. Assume a receiver is properly appointed in Texas, a non-UCRERA state. Assume further that, after conducting an investigation, the receiver identifies an apartment complex in Utah, a UCRERA state. What must the receiver do to take control over the apartment complex when the receiver's power and authority is jurisdictionally limited to Texas? As always, the receiver must first engage local counsel. Represented by local counsel, the process then becomes relatively simple. The receiver must file an application to be appointed as an ancillary receiver in the Utah county where the prospected receivership property is located. That application must identify, explain, and attach as an exhibit the Texas order whereby he or she was appointed as a receiver. The application must further state that the receiver does not meet any of the Disqualifying Factors. Assuming he or she does not, the Utah court may then enter an order giving effect to the Texas receivership order and granting the re-

ceiver all the rights, powers, and duties in Utah that he or she has in Texas. And once the order is entered, the receiver can take control over the apartment complex in full compliance with all jurisdictional requirements.

But what if the receiver discovers certain equipment parked at the apartment complex that the receiver wants to subject to the Texas receivership? Fortunately, the analysis does not substantively change. As noted above, UCRERA defines "property" to include both real *and* personal property so long as the personal property is "related to or used in operating the real property."[10] Accordingly, upon appointment by the Utah court, the Texas receiver can exercise control over the apartment complex and the equipment as an ancillary receiver in Utah.

Non-UCRERA States

What about assets in non-UCRERA states? Is the receiver out of luck in that instance? Not necessarily. Although only eleven states have so far adopted UCRERA, at least two others already have statutory provisions providing for ancillary receivers: Washington and Minnesota. Prior to the adoption of UCRERA, Washington and Minnesota were the only two states with comprehensive statutory frameworks covering receivers and receivership procedure.[11] As a result, the Conference adopted and UCRERA now mirrors several of those states' provisions, including those addressing ancillary receivers.[12] For example, under the Washington Code, a receiver appointed by a court of another state may be appointed by a Washington court to exercise control over receivership property located in Washington. Assuming the receiver is eligible for such appointment, a Washington court will enter an order giving effect to the receivership appointment order entered in the different state.[13] Minnesota has similar provisions. A Minnesota court may appoint a receiver appointed in a different state to exercise dominion over receivership assets in Minnesota, provided that the receiver is eligible and the appointment would further purposes of the out-of-state receivership.[14]

And even if a state has no specific statutory scheme covering ancillary receivers, an out-of-state receiver can likely file an action in the state court where the assets are located and ask that court, pursuant to the doctrines of comity and full faith and credit, to appoint an ancillary receiver in aid of the primary receivership.[15] If appointed, the ancillary receiver would derive its powers from that court's orders and would report to that court with respect to assets within that court's jurisdiction. Thus, even when operating in non-UCRERA states, a receiver appointed in one state who has assets to administer in another state will want to consult that state's statutory and common law for guidance on how to administer those out-of-state assets.

A decision from the Supreme Court of Idaho in 2017 is illustrative. In *Wechsler v. Wechsler*, the plaintiff obtained a receivership order in New York as a result of her ex-husband's failure to transfer funds according to a divorce judgment.[16] The plaintiff subsequently moved for the appointment of an ancillary receiver in Idaho to assist the primary receiver appointed in New York in marshalling the assets and property of the ex-husband in Idaho.[17] The district court ultimately granted the motion and appointed an ancillary receiver in Idaho to assist the primary receiver appointed in New York.[18] Citing the Idaho receivership statute, the ex-husband argued that the district court abused its discretion because: 1) its actions in appointing an ancillary receiver were not supported by Idaho statutory or case law; and 2) the authority granted to the ancillary receiver had already been granted to the primary receiver in New York.[19]

The Idaho Supreme Court found those arguments unconvincing. Although Idaho's statute does not use the specific term "ancillary receiver," the Supreme Court found that it authorized the appointment of an ancillary receiver.[20] The decision was largely left to the discretion of the district court.[21] And under the circumstances of the case, the Supreme Court opined that the district court had adequately articulated the need for an ancillary receiver and did not abuse its discretion.[22] Thus, despite the existence of a primary receiver in another state and no particular statute addressing ancillary receivers, the Idaho Supreme Court permitted the appointment of an ancillary receiver to address Idaho assets in order to assist the primary receiver in New York in marshalling the assets of the receivership estate.[23]

Federal Receiverships

A receiver appointed by a federal court has a much more streamlined path to follow to get control of assets in another state (or more specifically, another judicial district). Under federal law, "[a] receiver appointed in any civil action or proceeding involving property, real, personal or mixed, situated in different districts shall, upon giving bond as required by the court, be vested with complete jurisdiction and control of all such property with the right to take possession thereof."[24]

But there is a statutory deadline that can cause headaches for federal receivers and pose potential problems that a receiver would not likely encounter with UCRERA. The federal statute provides that "[s]uch receiver shall, *within ten days* after the entry of his order of appointment, file copies of the complaint and such order of appointment in the district court for each district in which property is located. The failure to file such copies in any district shall divest the receiver of jurisdiction and control over all such property in that district."[25] (Emphasis added.)

Therefore, for federal receivers who want to obtain control over property in another judicial district (not just another state) or to sue in another judicial district, they need to file their order of appointment and the complaint in that district within ten days.

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While the statute is quite clear that failure to file the order and complaint deprives the receiver of jurisdiction and control over the property outside the district of his appointment, courts have created an escape procedure if that is not done.

A receiver, of course, may not know what assets exist outside the district of his or her appointment or what claims he or she may have to assets outside the district within ten days of appointment. That information may only be learned after the receiver has conducted an investigation into the assets and liabilities of the receivership estate.

As a "work around" to this problem given the statutory language, a number of courts have indicated that if the receiver obtains an order "reappointing" the receiver he or she can file the reappointment order and the complaint in the foreign judicial district within ten days of the reappointment order and satisfy the statutory requirements.[26] As explained by the U.S. Court of Appeals for the District of Columbia Circuit: "On remand the court, the court may reappoint the receiver and start the ten-day clock of § 754 ticking once again."[27] While many courts have approved this escape hatch when the ten-day period is not met, one has to wonder how the U.S. Supreme Court would deal with it given its tendency to strictly construe statutes. Nevertheless, unless and until that issue makes its way to the Supreme Court (or is fixed by Congress), the escape procedure appears to continue to be a viable option for federal equity receivers.

Finally, while there are certainly key differences between equity receiverships and commercial receiverships, a commercial receiver in a federal diversity case might be able to take advantage of UCRERA's provisions if the district in which the federal court sits is in a UCRERA state. Under the *Erie* doctrine, the U.S. Supreme Court has long held that federal courts sitting in diversity must apply state substantive law and federal procedural law.[28] Because UCRERA likely constitutes substantive law, federal courts sitting in diversity should follow and apply UCRERA if the governing state law includes UCRERA. If UCRERA applies in a federal commercial receivership, then the receiver should be able to take advantage of the statute's various beneficial provisions, such as a statutory automatic stay and the ability to sell assets free and clear of liens. However, it may be that the provisions cited above requiring the receiver to act within ten days of appointment to secure out-of-district assets are procedural not substantive requirements. Therefore, even if a federal commercial receiver intends on using UCRERA's provisions, best practice would be to act promptly and follow federal statutory requirements to file copies of the complaint and appointment order within ten days of the receiver's initial appointment.

Conclusion

As soon as a receiver determines that receivership property exists outside of the state of initial appointment, he or she must first ascertain whether or not the second state has adopted UCRERA. If it has, the process becomes simpler and more streamlined. If it has not, and the second state is neither Minnesota or Washington, the process may be more complex and clunky and will require an in-depth investigation into state statutory and common law. But even then, courts have generally allowed for the appointment of ancillary receivers when the purposes behind the appointment have been adequately articulated by the prospective ancillary receiver. Thus, whether by statute or case law, a prospective ancillary receiver is likely to obtain appointment in a second state if he or she follows the procedures set forth above.

ENDNOTES

1 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 page 1, 6

2 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 page 2

3 https://www.uniformlaws.org/committees/community-home?CommunityKey=f8e2d89b-f300-40eb-a419-ad41902fcad2.

4 https://www.uniformlaws.org/committees/community-home?CommunityKey=f8e2d89b-f300-40eb-a419-ad41902fcad2

5 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 pages 4-5, 38, 45, 50-52.

6 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 page 71-72

7 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 pages 29, 71-72. "The court may appoint a receiver appointed in another state, or that person's nominee, as an ancillary receiver with respect to property located in this state or subject to the jurisdiction of the court for which a receiver could be appointed under this [act], if: (1) the person or nominee would be eligible to serve as receiver under Section 7; (2) the appointment furthers the person's possession, custody, control, or disposition of property subject to the receivership in the other state."

8 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 page 11

9 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 pages 71-72

10 Utah Code Ann. § 78B-21-104(1).

11 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 page 2

12 https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=181bdb28-c28e-162f-5bcc-00103dc1eb0a&forceDialog=0 pages 2 and 72

13 "A receiver appointed by a court of another state, or by a federal court in any district outside of [Washington], . . . may obtain

appointment by a superior court of [Washington] of that same receiver with respect to any property or business of the person over whose property the receiver is appointed constituting property of the foreign receivership that is located in this jurisdiction, if the person is eligible under RCW 7.60.035 to serve as receiver, and if the appointment is necessary to the receiver's possession, control, or disposition of the property in accordance with orders of the court in the foreign proceeding. The superior court upon the receiver's request shall enter the orders, not offensive to the laws and public policy of [Washington], necessary to effectuate orders entered by the court in the foreign receivership proceeding." Wash. Rev. Code Ann. § 7.60.270(2).

[14] "A foreign receiver may obtain appointment by a court of [Minnesota] as a receiver in an ancillary receivership with respect to any property located in or subject to the jurisdiction of the court if (1) the foreign receiver would be eligible to serve as receiver under section 576.26, and (2) the appointment is in furtherance of the foreign receiver's possession, control, or disposition of property subject to the foreign receivership and in accordance with orders of the foreign jurisdiction." Minn. Stat. Ann. § 576.41(2).

[15] *See, e.g.*, *Bodge v. Skinner Packing Co.,* 115 Neb. 41 (1926).

[16] *Wechsler v. Wechsler*, 162 Idaho 900, 905, 407 P.3d 214, 219 (2017)

[17] *Id*.

[18] *Id*.

[19] *Id*. at 214, 224.

[20] *Id*. at 224.

[21] *Id*. at 225.

[22] *Id*.

[23] *Id*.

[24] 28 U.S.C. § 754.

[25] 28 U.S.C. § 754.

[26] *See, e.g., SEC v. Vision Commc'ns, Inc.,* 74 F.3d 287, 291-92 (D.C. Cir. 1996).

[27] *Id*.

[28] *E.g., Hanna v. Plumer*, 380 U.S. 460, 465, 85 S. Ct. 1136, 1141, 14 L. Ed. 2d 8 (1965).