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Receiver's Role

Who plays this part in the distressed property drama?

by Jennifer Tullius and Jonathan Littrell

Within the chaos of foreclosures and deeds in lieu, lenders are utilizing receivers to minimize losses, maximize property values, and reduce potential liability on properties in default. It is no great surprise that an ever-growing number of commercial real estate professionals are expanding their résumés to include receivership to capitalize on this trend. What is surprising, however, is the apparent lack of understanding of the actual role, benefits, and drawbacks of appointing a receiver over real property.

Landing the Part

In most states, a real estate receiver is a court-appointed individual who is given custodial responsibility over real prop-

erty that serves as collateral for a loan in default. Once appointed by the court, the receiver completely displaces the borrower and becomes responsible for the tangible and intangible assets related to the property. Owing a fiduciary duty to the court and parties involved in the litigation, the receiver makes all decisions regarding management and operations, including leasing, improvements, and in some cases, positioning the property for sale.

Receivers' fees and fees for third-party professionals hired by the receiver typically are paid out of available cash-flow from the property's operations. If the property is cash negative, the lender often will advance funds to pay the receiver's fees.

That amount is then added to the borrower's principal loan balance.

Learning the Lines

A receiver's primary duty is to secure the property, prevent waste, and collect rents. In general, the receiver is required to follow the court's order, which may include specific authority to manage the property, collect rents, and provide monthly accountings. In some instances, the court may grant the receiver authority to enter into leases and position the property for sale.

Once appointed, the receiver must take custody of the property, which may include changing locks, securing operating accounts, and retrieving property-related documents from the borrower. Depending on the situation, obtaining control can be rather simple or very difficult. The key for the receiver is to act quickly so that the borrower cannot cause harm to the property.

After securing the property, the receiver should promptly inspect it and prepare a report summarizing the property's general condition and itemizing personal property of the borrower. The receiver also should send a letter to the tenants notifying them of the change in control, providing a new point of contact, and, ideally, arranging a time to meet with them individually to establish a relationship and discuss areas of concern.

Other items that generally require the receiver's immediate attention include the transfer of utility bills, placement of property insurance, hiring of a third-party management company, maintaining or entering



RECEIVERS BEWARE

The receiver's primary duty is to safeguard the property's assets, but he must not act beyond his authority or neglect his duties. For example, if the receiver has the power to sell the property, he or she should obtain court approval of the broker, the terms of the sale, and the buyer. Likewise, property improvements, especially those requiring large capital expenditures, require court approval. If a receiver intends to bring a lawsuit to protect, recover, or obtain possession of assets belonging to the receivership that are in the hands of another party, again he or she needs court approval. Failure to do so may result in the other party bringing a lawsuit against the receiver.

Receivers also can be held liable if they fail to comply with the orders of the receivership court. Liability may not be limited to a civil lawsuit; it could also result in criminal action if the receiver's conduct is found to be illegal by the court.

Other potential concerns include failing to obtain adequate insurance to protect the receivership assets, taking possession of assets that are not the property of the receivership estate, or transferring receivership property to a party not entitled to receive the property or where the receivership court has not approved such transfer.

When in doubt of what action should be taken, the receiver should always apply for instructions from the receivership court.

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into new service contracts with vendors, and other issues concerning the property's overall operation and security.

Upon termination of the receivership (generally as a result of a foreclosure, cure of the underlying default, or borrower's bankruptcy filing), the receiver will be required to file a final accounting and motion for order discharging the receiver.

Good Career Move?

Both the borrower and the lender typically benefit from the appointment of a receiver. More specifically, the borrower's liability will be reduced or in some cases elimi-

legal counsel and third-party management costs. However, because a receiver is typically a professional asset manager with strategic partnerships with third-party vendors, the property is more likely to become cash positive upon the appointment of the receiver, which in turn may reduce the amount of the lender's out-of-pocket expenses.

Another potential drawback is lack of control. Because receivers are agents of the court, their interests may not always align with the interests of the other parties. For example, if the receiver determines that it is in the best interest of *all parties* to sell the asset and the court agrees, the receiver may be granted

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nated, if the receiver is able to fully rehabilitate the property. The lender will benefit from the protection of the asset and possibly an increase in the asset's value that will decrease deficiencies.

Although the benefits of appointing a receiver generally outweigh the drawbacks, receivership can be a costly endeavor. In addition to the receiver's fees, there may be other professionals' fees such as the receiver's

authority to do so even over the borrower or lender's objection. However, maintaining open communication is a good way to ensure a lender's goals remain aligned with, or at the very least considered by, the receiver.

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