



To: All Policy Issuing Agents of WFG National Title Insurance Company

From: WFG Underwriting Department

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Subject: Uniform Commercial Real Estate Receivership Act

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## **I. What is the Uniform Commercial Real Estate Receivership Act?**

The Uniform Commercial Real Estate Receivership Act (UCRERA, or the Act) was drafted by National Conference of Commissioners on Uniform State Laws in July of 2015. It provides comprehensive statutory provisions for commercial receiverships.

As of August 2020, UCRERA has been enacted in nine states (Maryland, Arizona, Michigan, Tennessee, Nevada, Utah, Oregon<sup>1</sup>, North Carolina, and Florida).

Many states do not have well-established receivership laws already in place, and such laws tend to vary widely. UCRERA provides common standards to be used for commercial receiverships. Most importantly, it includes provisions by which lenders can enforce their security agreements without having to take on the business of the property owner, while maximizing the value of the property.

## **II. What is a Receiver?**

A receiver is a court-appointed officer who acts as a neutral party to manage property and assets of an ongoing business that is the subject of legal proceedings. In addition to managing the daily affairs of the business, the primary function of a receiver is to efficiently preserve business assets and to assist with liquidating portions of the business, if necessary.

## **III. What are the problems faced by commercial lenders?**

The economic crisis caused by the COVID-19 virus is unlike anything the United States has seen in recent memory, including problems caused by the mortgage crisis of 2007-2008. Commercial properties have particularly been affected. Retail space rentals, already hurt by the activities of a handful of major online vendors, have been battered as shopping malls and restaurants are left empty or underused.

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<sup>1</sup> Note: The Oregon Receivership Code (the "Code") applies to receiverships commenced on or after January 1, 2018 and provides a comprehensive scheme for a court appointed receiver to manage the real and or personal property of a person or a business. The Code applies to both **residential and commercial property**.

Commercial office space may never recover from the trend of allowing employees to work out of their home offices. Commercial construction, real estate development, and property management businesses have all been affected by the downturn.

Some lenders for commercial properties now find themselves in a difficult position. Although they may hold mortgages, deeds of trust, or other interests secured by real property, the traditional remedy of foreclosure is not adequate to fully protect their interests. This is because the real property may be a necessary component of an ongoing enterprise, without which revenues will suffer. Absent an effort to manage the primary business, the value of the secured collateral may plummet. As a rule, lenders do not want to be burdened with the costs, and liabilities associated with the property.

#### **IV. Benefits of appointing a Receiver:**

Instead of (or in addition to) foreclosing on their security instrument, a receiver can maximize the value of the foreclosed asset by taking advantage of the equitable powers of the court to keep the business of the borrower from being disrupted by a foreclosure proceeding. It shifts many risks and burdens of an existing business from the lender to the court-appointed Receiver.

Note that appointing a receiver does not prevent the lender from opting for a foreclosure at a future date, if necessary. In that sense, a receivership may be the best of both worlds for the lender.

#### **V. Summary of Key Provisions of UCRERA:**

Many of the concepts in UCRERA will be familiar to those of you who deal with foreclosures or bankruptcies on a regular basis. For example:

- Section 3 requires notice and the opportunity for a hearing before a court may issue an order under the Act. However, orders can be issued without prior notice and a hearing if the circumstances require it, or if nobody requests a hearing.
- Under Section 14, an order appointing a receiver operates as a stay on any act, action, or proceeding to obtain possession of, exercise control over, or enforce a judgment against receivership property or to enforce a lien against receivership property.

What follows is a summary of other important UCRERA provisions. Note that this is a summary only, and readers are advised to thoroughly review the Act as adopted in your own state, since it may include state-specific provisions different from, or not included below:

#### **Section 4: EXCLUSIONS**

- UCRERA applies to a receivership of an interest in real property and any personal property related to or used in operating the real property.
- It does not apply to most improved, 1-4 dwelling units (residential properties), unless the properties are used as a part of a commercial enterprise.

#### **Section 5: POWER OF COURT**

- The court that appoints a receiver has exclusive jurisdiction to direct the receiver and determine any controversy related to the receivership or receivership party.

#### **Section 6: APPOINTMENT OF RECEIVER**

- The court may appoint a receiver before a judgment is entered, in order to protect a party that demonstrates a right, title, or interest in the real property, if the property has revenue-producing potential and is in danger of waste, loss, dissipation, or impairment.
- The court may appoint a receiver after a judgment is entered, in order to either carry the judgment into effect, or when an execution has been returned unsatisfied and the owner refuses to apply the property in satisfaction of the judgment.
- With respect to foreclosures, a receiver may be appointed:
  1. If appointment is necessary to protect the property from waste, loss, transfer, dissipation or impairment;
  2. If the mortgagor agreed in a signed record to appointment of a receiver upon default;
  3. If the owner agreed, after default and in a signed record to appointment of a receiver;
  4. If the property and any other collateral held by the mortgagee are not sufficient to satisfy the secured obligation;
  5. If the owner fails to turn over to the mortgagee proceeds or rents the mortgagee was entitled to collect; or
  6. The holder of a subordinate lien obtains appointment of a receiver for the property.

#### Section 7: **DISQUALIFICATION FROM APPOINTMENT OF RECEIVER; DISCLOSURE OF INTEREST**

- A receiver cannot be appointed unless he/she submits a statement to the court that they are not disqualified. Grounds for disqualification of a receiver exist if the person:
  1. Is an affiliate of a party;
  2. Has an interest materially adverse to an interest of a party;
  3. Has a material financial interest in the outcome of the action, other than compensation the court may allow the receiver;
  4. Has a debtor-creditor relationship with a party; or
  5. Holds an equity interest in a party, other than a non-controlling interest in a publicly-traded company.

#### Section 9: **STATUS OF RECEIVER AS A LIEN CREDITOR**

Upon appointment of a receiver, the receiver has the status of a lien creditor under:

- a. UCC Article 9 as to receivership property that is personal property or fixtures; or
- b. Under state recording statutes as to receivership property that is real property.

(This means that the receiver can establish priority not only against subsequent creditors, but also against prior, unperfected secured parties).

#### Section 10: **SECURITY AGREEMENT COVERING AFTER-ACQUIRED PROPERTY**

- Property that a receiver or owner acquires after appointment of the receiver is subject to a security agreement entered into before the appointment to the same extent as if the court had not appointed the receiver.

(This provision means that any security agreement entered into prior to the receivership that secures after-acquired property to that creditor is still valid as against the rights of the receiver).

#### Section 11: **COLLECTION AND TURNOVER OR RECEIVERSHIP PROPERTY**

- Persons who owe a matured debt that is receivership property shall pay the debt to or on the order of the receiver.
- Persons who have possession, custody, or control of receivership property shall turn the property over to the receiver.
- Persons who owe debts to the owner must pay the debts to the receiver instead.
- The court may hold someone in contempt for failure to turn over property to the receiver.

#### Section 12: **POWERS AND DUTIES OF THE RECEIVER**

A receiver may:

- Collect, control, manage, conserve, and protect receivership property;
- Operate a business constituting receivership property, including: preservation, use, sale, lease, license, exchange, collection, or disposition of the property in the ordinary course of business;
- In the ordinary course, incur unsecured debt and pay expenses incidental to the receiver's use, sale, lease, license, exchange, collection, or disposition of receivership property;
- Assert a claim, right, cause of action, or defense of the owner which relates to receivership property;
- Seek and obtain permission of the court concerning receivership property;
- Compel a person to submit to examination upon issuance of a subpoena;
- Engage the services of professionals to assist the Receiver in discharging his/her duties;
- Exercise any power conferred by the court.

With court approval only, a receiver may:

- Incur debt for the use of the receivership property other than in the ordinary course of business;
- Make improvements to the property;
- Use or transfer property other than in the ordinary course of business;
- Adopt or reject executory contracts;
- Pay compensation to the receiver;
- Recommend allowance or disallowance of a creditor claim;
- Distribute receivership property;
- Keep business records, and account for receivership property;

### Section 13: **DUTIES OF OWNER**

The owner must:

- Assist and cooperate with the receiver;
- Preserve and turn over all receivership property in its possession, custody or control;
- Identify all records pertaining to receivership property;
- Upon subpoena, submit to examination under oath by the receiver;
- These duties apply to entity officers, directors, managers, members, partners, trustees, or other person exercising power to control the affairs of the owner;
- Failure to comply may result in an award of damages against the owner, including attorney's fees and costs.

### Section 14: **STAY; INJUNCTION**

An order appointing a receiver operates as a stay on any act, action, or proceeding:

- To obtain possession of, exercise control over, or enforce a judgment against receivership property;
- To enforce a lien against receivership property.

Note that in an action to foreclose or otherwise enforce a mortgage, an order appointing the receiver does not act as a stay or injunction. Nor does it act as a stay on the following:

- Actions to maintain or continue to perfect an interest in receivership property;
- Commencement of criminal proceedings;
- Enforcement of a judgment other than a money judgment, by a governmental unit to enforce its police or regulatory power;
- Enforce tax liability of a governmental unit against receivership property.

### Section 16: **USE OR TRANSFER OF RECEIVERSHIP PROPERTY NOT IN THE ORDINARY COURSE OF BUSINESS**

With court approval, the receiver may transfer receivership property outside of the ordinary course of business by sale, lease, license, exchange or other disposition. Unless the agreement of sale says otherwise, a sale under this section is free and clear of the lien of the person that obtained appointment of the receiver, any subordinate lien, and any right of redemption. Such a sale is still subject to any senior liens, however.

Any transfer under this section does not require a public auction.

### Section 17: **EXECUTORY CONTRACTS**

With court approval, a receiver may adopt or reject an executory contract of the owner relating to receivership property.

A receiver may not reject an unexpired lease of real property under which the owner is the landlord, if:

- The tenant occupies the premises as the tenant's primary residence;
- The receiver was appointed at the request of a person other than the mortgagee; or

- The receiver was appointed at the mortgagee's request and:
  - The lease is superior to the lien of the mortgage;
  - The tenant has an enforceable agreement with the mortgagee or the holder of a senior lien under which the tenant's occupancy will not be disturbed;
  - The Mortgagee has consented to the lease; or
  - The terms of the lease were commercially reasonable at the time the lease was agreed to and the tenant did not know or have reason to know the lease violated the mortgage.

#### Section 20: **NOTICE OF APPOINTMENT; CLAIM AGAINST RECEIVERSHIP; DISTRIBUTION TO CREDITORS**

Creditors of the owner shall be given notice of the appointment of the receiver by first class mail and publication, as directed by the court. It must inform creditors of the date by which each creditor must file its claim, which must be submitted to the receiver. Unless the court orders otherwise, claims that are not timely submitted are not entitled to distribution from the receivership.

A creditor's claim must:

- State the name and address of the creditor;
- State the amount and basis of the claim;
- Identify any property securing the claim;
- Be signed by the creditor under penalty of perjury; and
- Include a copy of any record on which the claim is based.

The receiver may file an objection to the court with respect to any creditor's claim, stating the basis for the objection. The court will allow or disallow the claim according to the law of that state.

If the court determines the receivership property is not adequate to satisfy all creditor claims, it may require notice to only those creditors as the court directs.

#### Section 21: **FEES AND EXPENSES**

The court may award the receiver reasonable fees and expenses for performing his/her duties. The court may require these to be paid by the person who requested the appointment of the receiver, or the person whose conduct justified the appointment of the receiver.

#### Section 22: **REMOVAL OF RECEIVER; REPLACEMENT; TERMINATION OF RECEIVERSHIP.**

The court may remove a receiver for cause, replace a receiver who dies, resigns, or is removed, and discharge a receiver upon a finding that the appointment of the receiver was improvident or the circumstances no longer warrant continuation of the receivership.

#### Section 23: **FINAL REPORT OF RECEIVER; DISCHARGE.**

Upon completion of the receiver's duties, the receiver shall file a final report including all of the requirements in this section.

#### Section 24: **RECEIVERSHIP IN ANOTHER STATE; ANCILLARY PROCEEDING.**

The court may appoint a receiver appointed in another state as an ancillary receiver, so long as that person would be eligible to serve as a receiver in this state.

## Section 25: **EFFECT OF ENFORCEMENT BY MORTGAGEE**

A request by a mortgagee for the appointment of a receiver, the appointment of a receiver, or application by a mortgagee of receivership property or proceeds to the secured obligation does not:

1. Make the mortgagee a mortgagee in possession of the property;
2. Make the mortgagee an agent of the owner;
3. Constitute an election of remedies that precludes a later action to enforce the secured obligation;
4. Make the secured obligation unenforceable;
5. Limit any right available to the mortgagee with respect to the secured obligation;
6. Bar a deficiency judgment pursuant to state law against the owner;

Receivership property sold pursuant Section 16(c) of UCRERA is free and clear of the lien and the ability of the creditor to enforce an obligation that had been secured by the lien is subject to state law.

### **VI. Underwriting requirements for UCRERA transactions:**

1. UCRERA generally applies to commercial properties only.
2. When underwriting a purchase or sale with a receiver appointed under the provisions of UCRERA, obtain a docket of the UCRERA action, and copies of relevant orders from the Court.
3. Determine whether court orders have been made with or without prior notice to the owner and a hearing.
4. If notice has not been provided, the receivership action can possibly be attacked at a later date on constitutional grounds (state and federal due process concepts require notice and the opportunity to be heard).
5. Wait for the appeals period to run on any court order (typically for 30 days) unless you obtain written Underwriter approval otherwise.
6. Verify whether a foreclosure has been filed against the same property that is the subject of the Receivership action under UCRERA. Note that a receivership does not prohibit the foreclosing lender from foreclosing in a separate action.
7. Note that a receivership does not wipe out prior security interests in the property. In other words, a senior lien to the foreclosed mortgage still has to be dealt with as you would in any foreclosure action.
8. Verify that the borrower has not begun a bankruptcy proceeding.
9. Treat any transaction in which a receivership under UCRERA is pending to be an extra-hazardous transaction that requires written underwriter approval and continuing guidance.

### **VII: Conclusion:**

UCRERA is a welcome tool for administering commercial real estate receiverships. It provides lenders with another option for managing and liquidating its collateral, with a uniform structure that is currently missing in the laws of many states.

UCRERA is not a replacement for bankruptcy or for foreclosures, but can be a useful tool in preventing low-bidder results in the latter. We can expect that UCRERA will be adopted in many more states in the coming years.

**NOTE:** The information contained in this Bulletin is intended solely for the use of employees of WFG National Title Insurance Company, its title insurance agents and approved attorneys. Disclosure to any other person is expressly prohibited unless approved in writing by the WFG National Title Insurance Company's Underwriting Department. **The Agent may be held responsible for any loss sustained as a result of the failure to follow the standards set forth above.**