

MEMORANDUM

TO: Appointment and Powers of Real Estate Receivers Drafting Committee, Advisors and Observers

CC: Harriett Lansing, Richard Cassidy, Anita Ramasastry, Lane Shetterly, John Sebert, and Ben Orzeske

FROM: Thomas S. Hemmendinger and R. Wilson Freyermuth

DATE: March 18, 2014

RE: Summary of March 7 – 8, 2014 Meeting of the MAAPRER Drafting Committee

The Drafting Committee on a Model Act on the Appointment and Powers of Real Estate Receivers met on March 7 and 8, 2014 in Salt Lake City. Those attending were Commissioners Thomas Hemmendinger (Chairperson), John Burton, Steve Cawood, Ellen Dyke, Thomas Edmonds, Patricia Fry, Donald Mielke, Fred Miller, Rosemary Sackett, Mark Sandlin, and Gay Taylor-Jones; Reporter R. Wilson Freyermuth; ABA Advisor John Trott; ABA Section Advisors Jeffrey Allen, Kay Kress, and James Schwartz; and Observers Gordon Dunfee (California Receivers Forum), Kelley McConnell, William Hoffman, Cheryl Kelly, David Leta, Beverly McFarland (California Receivers Forum), Benjamin Reeves, Steve Sepinuck (American College of Commercial Finance Lawyers), and Jeffrey Smith. Observer Kenneth Jannen (ALTA) could not attend, but provided helpful written comments before the meeting, and these were shared with the group.

ULC President Harriett Lansing, Executive Committee Chair Richard Cassidy, Division Chair Lane Shetterly, and Executive Director John Sebert attended portions of the meeting. Staff Liaison Ben Orzeske could not attend.

We considered the Reporter's February 12, 2014 draft of the Model Act. As in our previous meetings, the discussion was extremely productive, with everyone contributing helpful and practical substantive comments and suggestions. It was especially gratifying that all Commissioners and so many highly-engaged Observers could attend.

Except where specifically noted, the positions stated in this memo are not final decisions based on formal votes. Instead they reflect the consensus on what the Committee wants the Reporter to include in the draft for the Committee's first reading at the ULC's 2014 annual meeting.

After introductions and housekeeping matters, the meeting went as follows:

1) Power to Sell (§§ 16 and 17).

- a) The current draft contains power to sell in three sections: § 12 (sale in the ordinary course of business); § 16 (receiver causing a foreclosure sale); and § 17 (sale outside the ordinary course of business). Section 17 has three Alternatives for transfers outside the ordinary course of business:
 - i) *Alternative A*: The receiver can sell property free and clear of the plaintiff's lien and all subordinate interests, including rights of redemption.
 - ii) *Alternative B*: If the receivership relates to the foreclosure of a mortgage or the enforcement of an assignment of rents, and if the mortgagor or assignor consented to a sale, the receiver can sell free and clear.
 - iii) *Alternative C*: The receiver can sell property free and clear of all liens and rights of redemption.
 - iv) *Alternative D*: A transfer would require consent of the owner and lienholders, unless law other than this Act allows the transfer.
- b) After discussion, the consensus was for the Reporter to revise § 17 as follows:
 - i) The section shall be expanded to apply to each use, sale, lease, license, or other transfer of receivership property outside the ordinary course of business. As in the current draft, such a transaction would require court approval after notice and a hearing. Also, as in the current draft, the Act shall not define "ordinary course of business" or attempt to impose particular standards, such as marketing efforts or appraisals.
 - ii) The Act should not create a right of redemption where one does not already exist. Therefore, only statutory rights of redemption that exist outside the Act are relevant.
 - iii) The existing Alternative B on foreclosure-related receiverships should be dropped.
 - iv) The next draft of the Act should have three Alternatives:
 - (1) *Alternative A*: The receiver can sell property free and clear of all liens and any statutory right of redemption, to the extent the court orders that the sale be free and clear.
 - (2) *Alternative B*: The receiver can sell free and clear of the interests of the party who obtained the appointment of the receiver and all subordinate interests, including any statutory right of redemption, to the extent the court orders that the sale be free and clear. However, the sale would be subject to senior interests unless they consent.

- (3) *Alternative C*: A transfer would require consent of the owner and lienholders, unless law other than this Act allows the transfer.
- v) Under new Alternatives A and B, the court has discretion on the degree to which a transfer is free and clear of liens. However, as in the current draft, to the extent a transfer is free of a lien, the lien will automatically attach to the proceeds of the sale.
 - vi) Under new Alternatives B and C, the Committee prefers that the lienholder consent requirement be limited to the holders of valid liens.
 - vii) Under new Alternative C, the owner’s consent is effective only if made after the appointment of the receiver.
- c) At last September’s meeting, the Committee directed the Reporter to include an Alternative that allows the receiver to cause the sale of the property in the same manner as the plaintiff would have outside of receivership. In preparing for this meeting, the Chair and the Reporter concluded that this Alternative worked better as a free-standing section (§ 16 in the current draft), because it would logically apply even in States that choose to leave the general power to sell outside the scope of the Act.
- i) However, after reviewing the text, the group expressed concern over the implications of a receiver conducting a foreclosure. The Committee voted 8-1 to strike it from the Act.
- 2) Scope (§ 3).
- a) Residential Real Property.
 - i) Following the Committee’s direction at last September’s meeting, the current draft excludes a single-family dwelling that is the owner’s primary residence and from which the owner does not collect or derive income. The Committee had two goals: first, to include mixed-use properties, such as farms, ranches, wineries, and motels where the owner also resides; and second, to prevent owners from gaming the system, e.g. by moving in to a factory or other commercial facility to prevent the appointment of a receiver.
 - ii) However, at this meeting many participants expressed concern over the finer points of the draft exclusion. For example, the draft does not necessarily produce the desired result if the owner charges rent to an adult child who has moved home, or if the owner takes work home from the office. One solution proposed was to impose a “primary purpose” test on the owner’s generating income on the property. Another was to coordinate this exclusion with the current definition of “residential real property” in the draft Home Foreclosure Procedures Act (“HFPA”).

- iii) The Chair will consult with the Chair of the HFPA Drafting Committee, Bill Breetz, follow up with ULC leadership, and then report back to the group.
 - iv) In connection with the scope discussion, Don Mielke suggested renaming the Act. This issue was deferred until the end of the meeting (see below).
- b) State Agency Regulation. The Committee considered a Style Committee “delta” on whether the defined term “state agency” should retain its inclusion of county and municipal agencies and decided that it should. However, the Committee suggested that the defined term should be changed to something less confusing, such as “governmental unit.”
- c) Style Delta. The Style Committee had questions about how the defined terms “property” and “receivership property” are used in this section. After discussion, the Committee prefers to leave those parts of this section essentially unchanged, in light of the Executive Committee’s charge that the Act focus on real estate receiverships.
- 3) Power of Court (§ 4).
- a) The Committee was generally comfortable with the drafting approach in this section, but some members asked that the Reporter consider whether the police power issue should be in the statutory text, rather than in the comments.
- 4) Standing to Seek Appointment of Receiver; and Grounds for Appointment (§§ 5 and 6).
- a) The Committee decided that § 6(a) should be modified as follows:
 - i) Paragraph (3) should be revised so that it applies in States that require or permit non-judicial foreclosures, to require a default under the mortgage or lease assignment, and to allow the appointment “as necessary” to protect the property or rents.
 - ii) Paragraph (4)(D) should be deleted as unnecessary and potentially troublesome.
 - iii) Paragraph (6) should be modified to eliminate the argument that it creates a right of redemption where one does not exist under other law.
 - b) The Committee decided that § 5 on standing is unnecessary and should be dropped.
 - c) Section 6(b) should be left in brackets for the next draft.
- 5) Identity of Receiver (§ 7).
- a) At last September’s meeting, the Committee directed the Reporter to redraft this section as a disclosure requirement, rather than as a disqualification rule. In preparing the draft for this meeting, the Chair and the Reporter developed concerns over the disclosure model, so the

current draft contains both models as alternatives. After discussion, the consensus of the Committee was to strike the disclosure model and return to the disqualification model.

- b) The Committee directed the Reporter to modify this section to add a requirement that the receiver certify that it is eligible to serve in light of the disqualification standards.
 - c) The Committee stood by its prior decision not to include a competence standard. Further, the Committee does not want to address moral fitness in the statute, but leave it to the court.
- 6) Turnover (§ 11).
- a) The Committee directed that the next draft address the collection of debts separately from the turnover of property, so that receivers could not use contempt powers to collect debts. Steve Sepinuck offered to provide a memo and suggested language on this.
- 7) Receiver's Powers (§ 12), including Employment of Professionals (§ 15).
- a) Following on the discussion of § 11, the power to collect debts should be explicit in § 12(a).
 - b) Consistent with the Committee's directions on § 17, the receiver's power to deal with property in the ordinary course of business should include use, sale, lease, license, or other transfer of receivership property.
 - c) Each paragraph of § 12(b) that deals with a power covered in other sections should be drafted in a parallel manner.
 - d) Section 12(b)(2) should be clarified, so that it addresses claims against the owner or against the receivership property.
 - e) As to employment of professionals, the Committee prefers the approach in § 15 and directed the Reporter to eliminate potential inconsistencies appearing in § 12.
 - f) The Committee asked the Chair and the Reporter to consider for the next draft whether the independence standard for professionals in § 15 should be the same as for receivers in § 7.
 - g) The Committee was comfortable with how § 12 addresses the receiver's power to incur debt.
- 8) Owner's Duties (§ 13).
- a) The Chair reported to the Committee that, for various reasons, it is not feasible to include receivers in the ULC's proposed Fiduciary Access to Digital Assets project. Based on this briefing, the Committee decided that this Section should require the owner to give the receiver access to digital assets, such as websites, social media pages, cloud computing systems, and cloud storage. Therefore, the next draft of the Act will include an affirmative

duty to provide information to the receiver.

- b) The Committee believes that § 13 does not need its own turnover provisions, because a receiver can invoke the sanctions of § 11 merely by making demand on the owner.

9) Automatic Stay (§ 14).

- a) In reviewing an interim draft of this Act, several members of the Joint Editorial Board on Real Property Acts expressed concerns over the breadth of the automatic stay. However, after discussion the Committee remains comfortable with the stay provisions in this draft.
- b) Subsection (e) of the current draft makes acts in violation of the stay voidable, rather than void. The Committee is comfortable with that policy choice, but directed the Reporter to allow the receiver or any party to ask the court for relief under this subsection.
- c) The current draft presents two different approaches for dealing with willful violations of the automatic stay—Alternative A (damages) and Alternative B (contempt of court). The Committee decided that the two should be combined into a single subsection.
- d) The Chair and the Reporter will consider whether the term “willful” needs to be defined or modified in the next draft.
- e) The Chair and the Reporter will also review § 14(d)(2), to ensure that it adequately addresses perfection of purchase-money security interests and continuation of UCC-1 financing statements.

10) Receiver’s Immunity (§ 19).

- a) The Committee decided that the *Barton* protections should apply both during and after the receivership, and that any suit against the receiver should be in the court that appointed the receiver. The Committee adopted Jack Burton’s suggestion that the statutory text provide enough of the *Barton* doctrine to educate practitioners and courts on the doctrine.
- b) The immunities should be not only what the common law provides, but also what equitable principles or statutory law provide.
- c) In cases where there is an ancillary receivership, the receiver should have the protections of the law of each State, but should not have an unfair advantage by mixing and matching different levels of protection among the States’ laws.

11) Receiver as Lien Creditor (§ 9).

- a) The Committee remained firm that this section should not create a “strong-arm” avoiding

power as under Bankruptcy Code § 544. However, the Committee reached only a limited consensus on how this section ought to be revised for the next draft.

b) Therefore, the Reporter will revise this section as follows:

i) As to personal property, it would subordinate unperfected security interests, as in UCC § 9-317. Therefore, if a creditor failed to perfect a security interest, its rights would be junior to perfected security interests, but senior to general unsecured creditors.

ii) As to real property, it would mirror what real property law does in a priority dispute between an attaching creditor and the holder of an unrecorded mortgagee. In many States, an attaching creditor is not a “purchaser” and therefore is subordinate to a prior unrecorded mortgage. In other states, however, an attaching creditor does have priority. The Act would not affect the existing rule in any jurisdiction.

c) The Reporter will also consider whether the title of the section ought to be changed.

12) Security Interests in After-Acquired Property (§ 10).

a) Time did not permit us to address all issues raised by this section, so for the next draft the Chair and the Reporter will review this section in light of the group’s comments.

13) Executory Contracts (§ 18).

a) The Committee was comfortable with how the Reporter implemented the drafting directions from last September’s meeting and with the Reporter’s proposals to deal with issues not fully discussed at that meeting (land sale contracts, time shares, and protections for residential tenants).

b) Subsections (g) and (h) should be clarified, so that they apply only where the owner is the landlord. There should be no particular restrictions on the ability of a receiver for a tenant to reject a disadvantageous lease.

c) The Chair and the Reporter will consider the issue of non-Act law that excuses the counterparty from accepting performance by anyone other than the owner, as in certain personal services contracts.

14) Ancillary Receiverships (§ 24).

a) The power of the court in subsection (b) to enter orders in furtherance of orders entered by another court is a useful power and should not be limited to ancillary cases.

b) The Committee felt that it would be helpful to see if the National Center for State Courts and

the Conference of Chief Justices would provide Observers for this project. The Chair will confer with the Executive Director on this.

15) One-Action and Anti-Deficiency Laws (§ 25).

- a) The Committee suggested some small changes to the draft text, but also directed the Reporter as follows. The next draft should not state that a sale of receivership property constitutes a foreclosure. Instead, the draft should state that, to the extent a sale is free and clear of a particular lien, the State's anti-deficiency law would apply to the debt secured by that lien. There should also be a legislative note on this topic.

16) Claims (§ 21).

- a) The Committee believes that all creditors known to the receiver should get notice of the receivership proceeding. In addition to notice by mail and publication, the Act should require the recording of the receivership order or a *lis pendens* in the real estate records. Thereafter, the court should have the discretion to dispense with a claims-filing process if it would not be productive.
- b) Time did not permit the Committee to address the draft's distinction between secured claims and unsecured claims.

17) Definitions (§2).

- a) The Committee made several suggestions to refine some of the definitions for the next draft.

18) Name of the Act.

- a) By consensus, the Committee decided to ask the Executive Committee to rename the Act "Model Act on Commercial Real Estate Receiverships." It was felt that this would facilitate enactment.

19) Enactability; Additional Observers.

- a) Everyone was mindful that the Act should be readily enactable, and throughout the meeting the group tested ideas and suggestions against enactability concerns.
- b) The Chair will follow up on the suggestion to add the National Center for State Courts and the Conference of Chief Justices as Observers.

20) Wrap-up and Next Steps.

- a) Although we did not get to every provision of the Act, we covered the most important ones and were able to give the Reporter sufficient direction in preparing the annual meeting draft.

- b) The Chair briefed the group on the purpose of our first reading at the ULC 2014 annual meeting and on how the ULC will conduct the first reading. This first reading is scheduled for July 16. The annual meeting draft is due at the ULC office by May 27. Before then, the Chair wants to circulate one more draft and a proposed issues memo for the annual meeting and solicit written comments. All comments should be directed to the Chair and the Reporter. The Chair might hold a brief conference call to deal with any open issues.