

Managing Property for a Receiver

by Bruce J. Bergman

In the current economy, foreclosures — and therefore receiverships — are increasing. Most receivers want managing agents who can aid them in carrying out their responsibilities.

To understand the important aspects of managing property for a receiver, it is essential to know what a receiver is, why a receiver is appointed, the special concerns and needs of a receiver, and how the receiver's role as the party in charge of a property may differ from that of the typical property owner.

A property manager's initial contact with a receiver will probably occur in one of two ways. When foreclosure action is begun on a property, the holder of the mortgage and the appointed receiver may decide to retain the current building manager, reasoning that he or she is most familiar with the building's operation and financial circumstances.

Alternately, however, the holder of the mortgage may believe that the building's manager was at least partially to blame for the financial troubles leading to foreclosure. If this is the case, the holder of the mortgage and the appointed receiver will probably discontinue the services of the original manager and seek a new manager to "turn the building around."

In either case, the property manager should know that the receiver is not engaged to solve the financial problems of the property, but rather is to maintain the building's value while the foreclosure is taking place.

Foreclosures are complex, highly technical proceedings that can take many months, or even years, to be concluded. What happens to the

property during the course of the lawsuit?

If the lender simply ignores the property during the action, the owner may pocket all the income for that period. Perhaps more disconcerting for the lender, the owner may allow the property to deteriorate during the foreclosure. Obviously, this endangers the lender's security, because a badly neglected building will bring a lower price at the foreclosure sale.

To alleviate these problems, most mortgages allow the plaintiff in the foreclosure action (the lender or mortgagee) to obtain a court order — usually without notice to anyone — appointing a receiver of the rents and profits of the building. Thus, if the foreclosing mortgagee believes that the property may decline in value during the action, or that the defaulting mortgagor (or other party in possession) may neglect the premises, or if the case is expected to be protracted, he may seek the appointment of a receiver to preserve the premises for the benefit of the plaintiff.

How the receiver comes into possession

Not surprisingly, receivers are most often sought for income-producing commercial and multifamily buildings, although they can be appointed for one- and two-family homes or in partnership disputes. The foreclosing mortgagee obtains a court order appointing a receiver approved by the presiding judge. The receiver then proceeds to "qualify," which in most jurisdictions requires the filing of an oath and a bond, the amount of which is fixed by the court. The bond is the promise of a surety company to

stand behind any defalcations of the receiver while the building is in his or her charge.

The receiver usually is, but need not be, an attorney. In some cases, the receiver is a property manager. He or she is an officer of the court, deemed to have a very high standard of conduct, who is not an agent or representative of the owner. After having qualified for the position, the receiver typically sends a "notice to attorn" to all tenants, advising them that all rent due or to become due is to be paid to the receiver or the receiver's agent if one has been selected.

Importance of the receiver's order of appointment

The specific duties and powers of the receiver directly affect the power of the managing agent. These duties and powers are governed strictly by the terms of the order of appointment. Obviously, it is critical that the receiver carefully study the order to determine the bounds of his or her authority. Regardless of whether or not the receiver does this, the managing agent should request a copy of that order to ensure that he or she does not inadvertently exceed the receiver's authority, lest the manager be unable to recoup an expenditure.

Many receivership orders will restrict the amount of money to be spent for any single repair, sometimes limiting the maximum expenditure to as little as \$500. If the receiver and managing agent inadvertently exceed the maximum amount allowed for a repair, they may not be reimbursed for the outlay.

Terms and bounds of the order

A typical order appointing a receiver will detail the authority of the receiver's managing agent. The following points will usually be included:

Before entering upon his or her duties, the receiver must execute and file with the clerk of the court an undertaking (bond) in a sum set by the judge, conditioned upon the faithful discharge of the receiver's duties.

As an officer or representative of the court, the receiver is held to standards that exceed normal business practices. Any gross error or misdeed on the receiver's part may not simply be attributed to the vicissitudes of "business." The receiver may be surcharged personally for mismanagement; if he or she cannot pay this surcharge, the surety may be required to pay on the bond. Moreover, the receiver could be censured by the court for any misconduct. Thus, to the extent that the receiver relies upon the managing agent, the latter must be especially scrupulous in the conduct of managing the building.

The receiver is directed to demand, collect, and receive from all occupants, tenants, and licensees in possession, or other persons liable therefor, all the rents due and unpaid or to become fixed and due.

Any monies due or to become due are paid to the receiver. The managing agent must determine the status of past-due rents at the time the receiver is appointed and collect the money for the receiver. A manager who was the managing agent for the former owner must be careful to retain no loyalty to the previous landlord. The property manager's obligation must be solely to the receiver. Moreover, a mortgagor in possession — that is, an owner who is the defendant in the foreclosure — has the same obligation to pay rent for his or her apartment or store as any other tenant.

Similarly, if the owner entered into a "sweetheart" lease for himself, a family member, friend, or partner at below-market rent, the managing agent will probably need to go to court to have the actual rental value fixed and collected.

The receiver is authorized to employ an agent to rent and manage the premises and to pay the reasonable value of such agent's servants out of the rents received.

To increase the receiver's efficiency, the attorney who prepares the receivership order will usually insert a clause giving the receiver the power to hire a managing agent. But not every order contains such a provision, either because the lawyer has chosen not to include it or because the judge has struck out the provision. Without specific authority, the receiver cannot engage a managing agent. If the receiver disobeys the order and engages a managing agent, the managing agent's fees may not be allowed.

Therefore, you should make certain that the receiver's order provides for the engagement of a managing agent before entering into an agreement with a receiver. If it does not, you should decline employment until the receiver arranges for modification of the order.

You will notice that compensation of the managing agent is to be based on "reasonable" value of the agent's services. "Reasonable" can be defined as customary compensation for similar services in your area. In some cases, conditions in the building may be such that the customary fee would be insufficient compensation; then, a negotiated fee may be in order. However, even if the receiver agrees to a negotiated fee, he or she should obtain the approval of the lender in advance, because ultimately the lender will be paying or absorbing the fee. It also is prudent to ask the receiver to

obtain an order of the court authorizing and sanctioning the agreed-upon fee as the reasonable value of your services. Remember, if there is any question as to reasonableness, the receiver and the managing agent may not be assured of collecting the agent's fee.

The receiver is authorized to make any reasonable and necessary ordinary repairs to the premises.

This phrase is preferred in a receivership order because it allows the receiver (and the managing agent) fairly broad latitude in maintaining the premises. Again, the terms "reasonable," "necessary," and "ordinary" could be open to interpretation. When a major repair is required, the receiver and managing agent should obtain the approval of the lender and, as an extra precaution, a court order authorizing that repair. Although the cited clause does not specify a maximum amount to be spent on any one repair, many orders, as previously noted, do set monetary limits. In such a case, the authority of the court must be obtained before spending more than the limit, or the managing agent may be held responsible for any amount exceeding the limit.

The receiver is authorized from time to time to rent or lease space facilities for terms not exceeding one year or such longer terms as may be required by the laws of Anytown, U.S.A.

There will invariably be a limitation on the duration of leases during the receivership. In most cases, this impedes the normal rental process, because commercial tenants usually request long-term leases. But because even a protracted foreclosure action seldom continues beyond a year or two, the property should not be burdened with long-term leases at the time of the foreclosure sale. The court seeks to make the property as mar-

ketable as possible at the foreclosure sale even though, if properly negotiated, such long-term leases could make the property more valuable. The key point for the managing agent to be aware of is that his or her efforts to rent space are controlled by the terms of the order.

Working with the receiver

Although there may not be a prolix formal contract, there are still points to be considered in working with the receiver.

Duration: The length of time spent working with the receiver will be difficult to project; the managing agent can probably expect to work for the receiver as long as the receiver is satisfied with the manager's services, or until the court discharges the receiver. Although the court can discharge the receiver before the foreclosure action is completed, usually the receiver — and hence the managing agent — is retained until the action is finally concluded. Unlike other lawsuits, a foreclosure ends not with a judgment, but with the actual foreclosure sale, which can be held any time after judgment is passed down, depending upon local practice and the nature of the particular litigation.

Compensation: Even without a formal contract, the matter of compensation cannot be left open. The managing agent should at least obtain a letter from the receiver recognizing the amount of the agent's fee. Remember, if a negotiated fee is expected, try to get a court order confirming the fee.

Utility and employment contracts: Usually the managing agent employs the required on-site personnel and signs contracts for utilities, cleaning services, rubbish removal, and similar services. The receiver, however, is ultimately responsible for such contracts and consequently may request that all contracts be in the receiver's name —

which is to the benefit of the agent.

Expenditures: When working for an owner, the managing agent expects the contract to limit expenditures, except perhaps in emergencies. In a receivership, both parties are bound by the order and will probably work together to agree upon most monies to be spent.

Maintenance of records: Although it is important for managing agents to always maintain careful records, it is especially important when working with a receiver. Because the receiver is a court officer and thus required to adhere to very high standards, he or she needs a comprehensive monthly report showing all income, preferably according to unit, as well as all expenditures. Because the receiver may be required to submit an account of all income and expenditures to the court at the conclusion of the receivership, usually without the aid of an accountant, the receiver must keep a coherent record of all transactions. Moreover, because the account is subject to judicial scrutiny, the receiver must be prepared to document the statement of income and disbursements. Thus, the wise managing agent is particularly thorough.

Reducing tax assessments: Most agreements between owners and managing agents specify that it is the managing agent's responsibility to seek a reduction from the taxing authority in case a property is overassessed or improperly taxed. The managing agent may also have that responsibility in working with a receiver; however, because most receiverships are of short duration compared to the amount of time needed to seek such a reduction, this seldom occurs.

Cooperation with real estate brokers: Because the receiver has an obligation to maximize the property's income, the managing agent should cooperate if the receiver wishes to

employ brokers to rent space.

Insurance: Even though the receiver is not the owner of the property, he or she has an insurable interest and must at least obtain sufficient fire and liability coverage, but this is not the managing agent's responsibility. The agent should be named in the policy, however; it should not cost the receiver more, and the agent would probably be named as a defendant in any negligence suit.

Security deposits: Many jurisdictions have very strict requirements concerning the segregation of tenants' security deposits and the interest to be earned on these accounts. The receiver is, of course, responsible for all security deposits. Although the managing agent may hold these deposits for the receiver, it is safer to turn them over to the receiver. In a lawsuit, responsibility for security deposits properly rests with the receiver.

Release at conclusion of action: If the receiver's discharge is by court order, his or her liability — and thus the exposure of the managing agent — should be concluded when the foreclosure action ends. However, many receiverships are concluded when the defaulting owner sells the property prior to a foreclosure sale. In such a situation, an actual closing occurs: the owner, buyer, and receiver settle all obligations, agree on a method of paying the receiver's commissions, and the receiver turns over all funds to the owner.

The alert receiver will demand a release from the former owner and new buyer. Although the release of the receiver can be expected to insulate the managing agent from any subsequent claims, it is wise for the managing agent to request that the receiver's release also specifically release the management agent.

Evictions at the premises: The receiver has a duty to preserve the property and collect the maximum

income possible. The receiver must be diligent in evicting tenants who don't pay rent on time or who remain as holdover tenants in premises where new leases would yield higher rent. Obviously, the managing agent must keep a close watch on such situations and keep the receiver apprised. However, the managing agent cannot feel free to hire counsel for such legal matters as would otherwise be usual, because the receiver, and thus the managing agent, may not have been given that authority by the order of appointment.

Caution on expenditures

When working for a typical property owner, the managing agent usually knows what repairs and maintenance the owner would like performed on the property. The owner is in a position to make a business judgment (often aided by the advice of the managing agent) about upkeep or improvements and is free to seek additional financing if the current cash flow won't support a specific program.

Such is not the case with a receiver. The receiver is charged with preserving the property, not improving it—at least not in the sense of capital improvements. But sometimes a property's income is not sufficient to support even minimal maintenance. In such a case, the only possible source of funds is the plaintiff in the foreclosure action — the lender. Whether or not the lender is prepared to make any advances is problematical.

In any case, it is critical for the managing agent to realize that, for the most part, his or her professional efforts are severely constricted by the availability of funds. The fact that the situation is not "normal" must always be borne in mind.

Any zealous attempt by the receiver or managing agent to proceed on a deficit basis — which might be quite acceptable in an owner-manager

situation — could cost either or both of them money from personal funds. Therefore, again, caution is in order.

Understanding the receiver's commission

As an officer of the court, the receiver is rendering a public service. But he or she is compensated, and it is important for the managing agent to be aware of the receiver's concerns in this regard, because the managing agent's actions affect the amount the receiver is paid. Exactly how much a receiver is to be paid is set by the laws of each state, subject to court interpretations of the statutes. In general, however, the receiver is paid a commission based on the amount of money — both income and expenditures — for which the receiver is responsible.

Accepting an engagement from a receiver can certainly be financially rewarding to a managing agent, but the managing agent must understand that there are significant differences between managing a building for an owner and managing for a receiver. Armed with a working knowledge of those differences, the managing agent can enter a new and important area of the real estate profession.



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