

## Receiverships May Be Particularly Useful For New Industries

By **Ira Bodenstein and Brian Soper** (December 19, 2018, 2:56 PM EST)

In today's business and financial marketplace, receiverships should be considered as an alternative for troubled businesses facing insurmountable balance sheet issues. For businesses that become embroiled in contentious or potentially fraudulent issues with little or no hope of surviving as an ongoing concern, receiverships can serve as a viable and cost-effective strategy for resolving debt and addressing business challenges.

Receiverships are prevalent in industry sectors where fraud and corruption are on the rise. New or existing industries that are susceptible to potential fraudulent activity and not highly regulated are likely to see an increase in these issues, and when they occur, a receivership can be an advantageous approach to recover and restore value for the estate and its beneficiaries.

In addition to Ponzi schemes, securities and real estate fraud, receiverships have been increasingly employed in matters involving cryptocurrency, as well as involving fraud surrounding the EB-5 immigrant investor program. They also are commonly seen in scenarios where a business owner is running the company into the ground and the secured creditors or other involved parties intervene to "right the ship" through a court-appointed receivership.

### The Role of the Receiver: Protect and Preserve

Generally speaking, the role of the receiver — a professional appointed by the state or federal court — is to administer and/or liquidate the estate of a troubled entity. In many ways, their role is comparable to a trustee in a bankruptcy proceeding, however they often have greater flexibility to perform their duties with a wider array of actions and strategies under a more simplified framework and process, all as dictated by the court order and presiding judge.

The primary duty of the receiver is to protect the interests of stakeholders and preserve the value of the receivership estate through the means granted to them based on the local jurisdiction, the judge overseeing the matter, the receiver's appointment order as well as the circumstances of the case. In essence, a receiver serves as a fiduciary who helps to recover value for the company and its creditors.

Depending on the parameters of the appointment order, a receiver may work in tandem with a small



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team of professionals under his or her supervision to untangle the affairs of the company. Receivers may hire experts to assist with forensic accounting and data mining that is necessary to locate a breadcrumb trail to the clues to a Ponzi or other fraudulent scheme that has been at the epicenter of a company's demise. If they are not themselves a practicing attorney, they may hire one as well as an accountant to help manage the legal and financial affairs of the receivership estate.

Among their numerous duties as set forth in the appointment order, receivers must assess the viability of the company as a going concern, the investments that creditors have made, whether they have been repaid and develop a strategy to recover and disburse what is owed to them. The strategies they use in achieving this goal vary greatly depending on the powers granted in their appointment order and discretion of the court in approving the receiver's requests.

### **Regulatory Versus Nonregulatory Receiverships**

There are two general categories of receiverships — federal equity receiverships, initiated by a regulatory agency, which are also known as regulatory receiverships, and federal and state court-appointed receiverships, commonly referred to as non-regulatory receiverships.

The defining characteristic between these two types of receiverships is whether or not a regulatory agency is involved in appointing the receiver, such as the Securities and Exchange Commission or the Federal Trade Commission, based on a violation of the rules and regulations of these federal agencies, which are in place to protect interests of individuals under federal regulations and laws.

In layman's terms, the nonregulatory receivership would have no "alphabet agencies" involved, but instead would be appointed by a federal or state court or initiated by a secured creditor or other involved party. These might be cases involving high-asset divorces, business partnership disputes and situations where businesses have lost their licenses and no longer have the management and authority in place to wind-down their operations. Real estate receiverships also tend to be nonregulatory matters.

Within the regulatory and nonregulatory categories, there are other more specific types of receiverships that may be put into motion, which depend on the situation at hand and the scope and authority granted by the court or regulatory body. In essence, every receivership is different based on the needs of the case.

### **Best Practices and Considerations**

In carrying out their appointed duties as agents of the court, receivers are required to operate within the guidelines provided by the appointment order and the presiding judge. While receiverships can provide a great deal of flexibility and considerable latitude in resolving matters, it is essential that the receiver does not act outside the duties delineated in the appointment order in fulfilling their various roles and responsibilities. The National Association of Federal Equity Receivers is an excellent resource on best practices in a receivership.

Within nonregulatory receiverships where a federal agency has not initiated the process, receivers must still coordinate with government authorities when they are involved and ensure they are in compliance with federal priority statutes. For example, the IRS may play an active role in the matter or there may be a companion criminal investigation underway with the Federal Bureau of Investigations.

When comparing the differences between receiverships and other forms of insolvency proceedings

including bankruptcy and assignments for the benefit of creditors, legal professionals should consult with their teams and experts to fully understand how these differences will play out in each situation. There are scenarios that are best-suited for bankruptcy where putting a receivership in place may not be the best fit. For example, a conventional bankruptcy process may be more appropriate if there are significant number of preferential transfers which are recoverable in a bankruptcy, but not in a receivership.

However, many creditors and lenders will seek receivership when there are not adequate funds or assets available to fund a bankruptcy proceeding, but there is still a need to recover assets and repay creditors. Furthermore, some creditors may find receiverships to be advantageous because there are no preference recoveries.

As receiverships become increasingly common, the role of technology to streamline the process for all involved parties should not be overlooked or underestimated. Technology and software resources can allow receivers to administer their matters and engagements more efficiently.

In fulfilling their duties, receivers have an ongoing need to find the optimal depository options for recovered assets. Technology can help them do this and enable them to track these assets and other details related to the properties in the case. They can also manage creditor information by creating a database of what was invested and what must be recovered and paid to them. By using a technology platform tied to their banking institution, receivers can manage everything they need through one dashboard, which ultimately reduces the time and cost of the process while maximizing returns to creditors.

Receiverships are not new, but now more than ever, they provide a potential remedy to resolve debt and financial distress among troubled enterprises and entities when bankruptcy is not a viable option. Legal professionals from all disciplines can benefit from a deeper understanding of receiverships to consider them as an alternative or parallel solution to support complex litigation and restructuring matters.

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