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Picking Your Poison: When and How to Seek Appointment of a Receiver for Borrower Defaults

Thomas M. Whelan

Author Contact Information:

McGuire, Craddock & Strother, P.C.

Dallas, TX

twhelan@mcsllaw.com

214.954.6815

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I. INTRODUCTION

In Texas, non-judicial foreclosure and the other self-help remedies available to a mortgage lender for a borrower's default are generally quick, easy, and cheap. But this outline focuses on receiverships and other judicial remedies that are slow, hard, and costly. Why? Despite such practical disadvantages, resort to judicial remedies becomes necessary whenever a mortgage lender's non-judicial remedies are inadequate to preserve or protect the lender's collateral. In many cases, the inadequacy of a mortgage lender's legal remedies is itself a predicate to a court appointing a receiver or granting other equitable or extraordinary judicial relief. This outline will achieve its purpose if it serves as a practical refresher on the substantive law and procedural rules governing the appropriate use of receiverships and other judicial remedies when circumstances warrant.

Such a refresher appears in order. During the now decade-long bull run in the real estate market, mortgage loan defaults have been relatively few. Predictions vary on whether high inflation and rising interest rates will cripple the bull or even slow its run. In any case, let's hope for the best and prepare for less than the worst. The worst, of course, is bankruptcy, which is beyond the scope of this outline.

II. RECEIVERSHIP

A "district court has broad discretion in appointing a receiver, [and] it may consider a host of relevant factors, and [] no one factor is dispositive."¹ Simply put, there is no "precise formula for determining when a receiver may be appointed."² Because appointment of a receiver is such a harsh remedy,³ however, it ordinarily is a judicial remedy of last resort.⁴

A. GENERAL EQUITABLE STANDARD FOR APPOINTMENT OF A RECEIVER.

In deciding whether to exercise their inherent equitable powers to appoint a receiver, federal district courts in the Fifth Circuit consider the following factors:

- the existence of a valid claim by the party seeking the appointment;
- the probability that fraudulent conduct has occurred or will occur to frustrate that claim;
- imminent danger that property will be concealed, lost, or diminished in value;
- inadequacy of legal remedies;
- lack of a less drastic equitable remedy; and
- likelihood that appointing the receiver will do more good than harm.⁵

A similarly heavy burden rests on a party asking a Texas trial court to exercise its inherent equitable powers to appoint a receiver.⁶ If the applicant for a receiver demonstrates that no other available legal or equitable

¹ *Canada Life Assur. Co. v. LaPeter*, 563 F.3d 837, 844 (9th Cir. 2009) (quoting *Aviation Supply Corp. v. R.S.B.I. Aerospace, Inc.*, 999 F.2d 314, 316 (8th Cir. 1993)).

² *Canada Life Assur. Co.*, 563 F.3d *Id.* at 845.

³ *Indep. Am. Savs. Ass'n v. Preston 117 Joint Venture*, 753 S.W.2d 749, 750 (Tex. App.—Dallas 1988, no writ) (stating that "[r]eceivership is an extraordinarily harsh remedy and one that courts are particularly loathe to utilize.").

⁴ *U.S. Bank Nat'l Ass'n v. Grayson Hosp., Inc.*, No. 4:14CV570, 2014 WL 7272842, at *2 (E.D. Tex. Dec. 22, 2014) (citing *Santibanez v. Wier McMahon & Co.*, 105 F.3d 234, 241 (5th Cir. 1997) and holding that "a receivership is not necessary if [lender's] interests are adequately protected" and would be so protected if borrower related parties "deposited \$6 million in the Registry of the Court").

⁵ *Santibanez*, 105 F.3d at 241 (stating also that "where the appointment of a receiver is sought at the commencement [of the suit] . . . [t]he decision will be made on the basis of the moving papers and such answers, affidavits in opposition, or counter-affidavits as may be offered, and also on the testimony of witnesses in open court if the court deems such a hearing advisable.").

⁶ *See, e.g., Parness v. Parness*, 560 S.W.2d 181, 182 (Tex. Civ. App.—Dallas 1977, no writ) (citations omitted):

It is well settled in Texas that the appointment of a receiver is a harsh remedy and should only be exercised in extraordinary circumstances. Only where the evidence shows some serious injury will

remedy will do the job—preventing irreparable loss or damage to an under-secured mortgage lender—a court might appoint a receiver.⁷

B. RECEIVER’S ROLE

A receiver is a person appointed as “an arm or instrumentality of the court, holding possession of property for the court which appointed him.”⁸ The “classic” duties of a receiver pending a foreclosure is to “receive and collect rents, assemble and preserve, to the extent necessary, said property covered by said mortgage; assemble and preserve all property covered by said mortgage which constitutes personal and movable property and see that said property is located on said premises and make reports as required by the Court of his performance of his duties”⁹ “A receivership in a foreclosure suit it [sic] limited and special. The rents and profits are impounded for the benefit of a particular mortgagee, to be applied upon the debt in the event of a deficiency. . . . There is neither winding up of the business nor attempt to reorganize it and set it going anew.”¹⁰ In carrying out the court’s limited charge, the person appointed as a receiver, as in all other receivership cases, must be disinterested,¹¹ equally representing and protecting “the interests of all persons, including creditors, shareholders and others, in the property in receivership.”¹² As Justice John Minor Wisdom put it, “[a] receiver by any other name, or by no name, is still a receiver.”¹³

C. FEDERAL OR STATE COURT?

Whether a typical mortgage lender can establish and maintain federal subject matter jurisdiction in a suit seeking appointment of a receiver poses a complex legal riddle far beyond the scope of this outline. Because appointment of a receiver in federal court is an ancillary remedy for an underlying claim over

result to the applicant, or is threatened, will the drastic remedy of receivership be applied. Finally, a receiver should be appointed only in those situations where the property involved is in present danger of being lost, removed or materially injured and should never be ordered if another remedy, less harsh, is available which will afford the needed protection.

Id.; see also *Norem v. Norem*, 105 S.W.3d 213, 216 fn. 3 (Tex. App.—Dallas 2003, no pet.) (stating that *Parness* “appears to limit receiverships in temporary orders to property that is in present danger of being lost, removed, or materially injured and no other, less harsh, remedy is available that will afford the needed protection” but “does not refer to the family code [receivership] provisions” and concluding that “the standards and reasoning of *Parness* do not apply to setting standards of proof under the family code [receivership] provisions”).

⁷ *Canada Life Assur. Co.*, 563 F.3d at 844 (internal quotations and citations omitted); *World Fuel Sys. Corp. v. Moorehead*, 229 F.Supp.2d 584 (N.D. Tex. 2002); see also *View Crest Garden Apts., Inv. v. U.S.*, 281 F.2d 844, 847 (9th Cir. 1960) (stating that whether property is of sufficient value to satisfy debt and whether the obligors are solvent or of “doubtful financial standing” are weighty considerations).

⁸ *First S. Props., Inc. v. Vallone*, 533 S.W.2d 339, 343 (Tex. 1976) (citing *Farm & Home Savs. & Loan Ass’n v. Breeding*, 115 S.W.2d 615, 616 (Tex. 1938)); *Crites, Inc. v. Prudential Ins. Co. of Am.*, 322 U.S. 408, 414, 64 (1944); *Certain Underwriters at Lloyds London v. Perraud*, 623 F. App’x 628, 637 (5th Cir. 2015) (unpublished) (“[A] receiver is ‘not an agent of the parties,’ and is instead ‘considered to be an officer of the court.’” (quoting 12 Charles A. Wright & Arthur R. Miller, FEDERAL PRACTICE & PROCEDURE § 2981 (2d ed. 2015))).

⁹ *United States v. Sylacauga Props., Inc.*, 323 F.2d 487, 490 (5th Cir. 1963) (J., Wisdom) (citing *Duparquet Huot Co. v. Evans*, 297 U.S. 216, 221 (1936)).

¹⁰ *Sylacauga Props., Inc.*, 323 F.2d at 490 (quoting *Evans*, 297 U.S. at 221).

¹¹ *Davis v. Bayless, Bayless & Stokes*, 70 F.3d 367, 375 (5th Cir. 1995) (counsel for party to receivership proceeding is not eligible for appointment as receiver and will not qualify for judicial immunity as agent of receiver); TEX. CIV. PRAC. & REM. CODE § 64.021(a)(2) (stating receiver “must not be a party, attorney, or other person interested in the action for appointment of a receiver”).

¹² *Security Trust Co. v. Lipscomb Cnty.*, 180 S.W.2d 151, 158 (Tex. 1944); see also *Payne v. Snyder*, 661 S.W.2d 134, 143–44 (Tex. App. – Amarillo 1983, writ ref’d n.r.e.) (stating, as a general rule, that receiver represents all parties interested in litigation in which he is appointed and that receiver generally is agent of appointing court and not an agent of owner whose property is placed in receiver’s charge, except in certain circumstances under which receiver is held to be agent of property owner as a matter of law).

¹³ *Sylacauga Props., Inc.*, 323 F.2d at 487.

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