

Critical Components of an Effective “Order to Appoint a Receiver” – From the Lender’s Perspective

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It is inevitable – many hotels will go into receivership and/or foreclosure in the coming months. Some owners cannot afford to fight any longer, some lenders cannot kick the can down the road any longer, or any number of other reasons will start them down this path.

Receiverships can be extremely beneficial to the lender or they can be problematic. The three tools central to establishing a receivership which is beneficial to the lender are: 1) the right Receiver 2) the right Receiver’s attorney, and 3) a strategically drafted “Order to Appoint a Receiver.” This article addresses the third tool in a lender’s toolbox – the all-important court Order.



A Receiver is almost always put forward by the lender in the form of a motion as part of a foreclosure action and appointed by the Court (Judge) using an “Order to Appoint a Receiver” (or a similar name). For that reason, the Receiver “works for” or is answerable only to the Judge in the case. But it is the lender which submits a draft Order for the borrower’s attorney and the Judge to consider. Therefore, it’s essential that the lender’s proposed order conform to state law and include the Receiver’s rights, authority, and responsibilities that ultimately protect the asset (hotel) and benefit the lender’s position relative to the asset both during and after the receivership. The borrower and the Judge may both seek changes, and the final version is created via both legal arguments and negotiations in and out of the courtroom.

HVS has been appointed as Receiver for many hotels over the years, including both the 2001 downturn and the 2008 economic crisis, so our team’s experience has enabled us to develop the following list of the critical elements of an effective Order. Not all lenders’ attorneys have worked on hotel receiverships because of how long it has been since they were common so they might not know how powerful a properly structured Order can be for their client. HVS has numerous Motion/Orders which we share with prospective clients during discussions surrounding our appointment as a Receiver.

- Name as many entities, affiliates, and people related to the borrower as possible to include as broad a swath of assets as possible to be considered “Receivership Property”.
- The definition of Receivership Property (or Receivership Estate) should encompass all tangible and intangible property such as buildings, structures, leases, rents, fixtures, vehicles, and any moveable personal property located both on the land and elsewhere.
- Create a comprehensive list of Receiver powers, making sure to include the following in addition to otherwise standard powers:
 - ◊ Hire and terminate attorneys, consultants, security, service providers, restaurant operator, and hotel operator and pay them from the Receivership Estate

Summary

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- Hire a real estate broker to market the property for sale or lease
- Sell the property (upon Court approval)
- Make, modify, or terminate leases, agreements, or contracts (new leases, agreements, or contracts must be terminable at the end of the Receivership)
- Put any of the above in the Receiver's name
- Take possession of all current and future assets ("future" would be at any time during the term of the Receivership) and execute any document, instrument, or agreement to allow the Receiver to take possession and control those current and future assets.
- Freeze any bank or other accounts which the Receiver believes includes funds derived from the hotel, regardless of the name of the account and instruct the financial institutions to take direction solely from the Receiver
- Change locks or other security devices
- Issue Receiver certificates, with the permission of the Court, where permitted by state law, to finance its activities if other funding is unavailable (Note – A typical order gives the lender the right but not the obligation to fund the Receiver)
- Take any steps necessary to operate, protect, preserve the assets including life safety issues
- Issue demands and institute, continue, or resolve all proper legal actions to preserve or recover any funds or assets that may be due to the Receivership Estate which includes amounts due from the borrower
- Petition the Court for an Order to Show Cause (or similar) to find parties in contempt if they do not cooperate with the requirements in the Order to Appoint a Receiver.
- Suspend, limit, restart, or continue operations
- Affirmatively states that the Receiver has no obligation to settle or pay any debts, expenses, or liabilities which were incurred pre-Receivership, including utilities, payroll, or taxes of any kind.
- Affirmatively state that the lender will not have any liability for the acts or omissions of the Receiver.
- Allow the Receiver to secure a Receiver's bond instead of having to place funds on deposit with the court.
- The Receiver must maintain adequate casualty and liability insurance coverage for the Receivership Property, naming Receiver, borrower, and lender as insureds as appropriate.
- The Receiver should be required to obtain permission from the lender before spending more than \$x to replace (not repair) any of the physical assets. The amount of this threshold should be proportional to the size and scope of the hotel and the lender should consider how frequently its staff wants to be asked for this permission.
- Include a specific but also broad list of what the borrower is required to "surrender" to the Receiver both immediately and if they become in the borrower's possession, in addition to the Receivership Property secured by the mortgage. These items will be essential for the Receiver to operate and protect the Receivership Property – some examples are: financial records, sales records, all funds, original leases, contracts, insurance policies, sales and occupancy tax filings, security and other deposits, files/records, names of vendors/supplies, passwords, logins, and anything that the Receiver determines is necessary and relevant.
- The borrower must also provide the Receiver with the following:
 - Line-item level accounting of all revenue and expenses associated with the mortgaged property for 12 months prior to the date of the Order
 - General ledger report tied to that revenue and expense
 - Aged itemization and copies of all unpaid bills
 - Aged itemization and copies of accounts receivable
 - Details of all reservations, advance deposits, gift certificates outstanding and group / catering contracts
 - Maintenance records, as-built construction drawings, certificates of occupancy, licenses, permits, inspection records of any kind, copies or originals of personal files, payroll records
- The borrower should be restrained from doing the following without express written permission from the

Receiver:

- Interfering in any manner
- Communicating with employees, tenants, clients, bank, or vendors,
- Accessing the hotel at any time
- Removing, destroying, concealing, altering, or disabling any of the Receivership Property
- Redirecting mail or interfering in mail or express mail or packages or shipments
- Taking any action with respect to the control, use, operation, maintenance, leasing, or sale of the Receivership Property
- Require that all state and local authorities transfer all permits and licenses to the Receiver
- Require that the franchisor, if one exists, transfer, and not cancel, the franchise license to the Receiver (or execute a new, short-term one tailored to a receivership which can be terminated upon termination of the Receivership)
- The borrower must notify the Court and the Receiver within 24 hours of filing for Chapter 11 bankruptcy
- The Operator, if any, should be restrained from suspending, limiting, or restarting operations – this power rests with the Receiver.
- The Operator, if any, should be restrained from abandoning the hotel or terminating its management agreement on less than 60 days' notice.
- All funds in any account maintained by the Receiver remain as collateral for the benefit of the Lender and shall be paid to lender upon the termination of the Receivership if the outstanding debt has not been paid in full.
- Financial institution with funds or accounts determined by the Receiver to be part of the Receivership Estate must provide the Receiver a list of all account numbers, names, and monthly bank statements up to one year prior to the date of the Order.
- Any funds advanced by the lender to the Receiver to resolve a shortfall of funds to cover the Receivership shall be deemed an advance to the borrower and added to the outstanding loan balance, secured in the same manner as the loan.

Not all judges will agree to these items and certainly many borrower's counsel will object to some elements if given the opportunity. But, including them in the draft Order from the outset will put these powers and provisions, which are enormously beneficial to the lender's position, on the table for discussion and negotiation.

The foregoing list of recommended provisions is by no means comprehensive, nor does it provide the necessary legal language, but it does furnish the objective of the recommended provisions which a lender's attorney will find favorable for the client if he/she is new to this situation. Additionally, please note that, for the sake of brevity, this list intentionally excludes standard provisions such as case description, reporting, insurance, indemnification, compensation, and other core elements of a fully drafted Receiver order.

About **Victoria 'Vicki' S Richman**



Vicki Richman, CFO and COO of HVS Hotel Management and HVS Asset Management - Newport, has diverse industry experience including as Director, Consulting Services, Stephen W. Brener Associates, Inc., New York. She is a focused manager and analyst who is able to interpret information and deliver it a useful and comprehensive manner to the end users. She is a native of Newton (Boston), Mass. and has an undergraduate degree from Brown University and a Wharton MBA. Contact Vicki at +1 (401) 625-5017 or .