

# **CONSIDERATIONS IN A COURT-ORDERED RECEIVERSHIP**

**Part 1: Legal Basis under State Law**

**Part 2: Discussion of Receiver's Duties**

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# **Part 1: Legal Basis under State Law**

## **1. Definition:**

“Receivership” is an equitable remedy authorized by federal or state statute. The receiver is the person appointed by a court to take possession and to preserve property or a business that is involved in pending litigation, so as to protect the rights of the parties until the court reaches a final decision.

Authority for a state-court receivership may be found in Ala. Code §§ 6-6-620 – 6-6-628, and ARCP 66.

## **2. Alternative Remedies Under Federal Law**

- Assuming there is pending litigation in the federal court based on jurisdiction by federal question under 28 U.S.C. § 1331 or by diversity under 28 U.S.C. § 1332, the court has ancillary jurisdiction to appoint a receiver pursuant to 28 U.S.C. § 754.

A federal court will consider federal, not state, common law to decide whether to grant this equitable remedy. *Gordon v. Washington*, 295 U.S. 30 (1935).

- Petitioning creditors may seek to place a person or a for-profit business in an involuntary bankruptcy under Chapter 7 (liquidation) or Chapter 11 (reorganization) pursuant to 11 U.S.C. § 303. (Note that this statute does not apply to family farmers and non-profit entities.)

Appointment of a bankruptcy trustee may not occur as quickly as appointment of a receiver because the debtor can oppose the bankruptcy and demand a trial under § 303(h). However, prior to trial any party in interest can request a hearing to propose that the extreme circumstances require immediate appointment of a trustee to manage and preserve the property or business of the debtor under § 303(g).

## **3. The Appointment Process**

### **a. When A Receivership is An Appropriate Equitable Remedy**

- It is always ancillary to the primary relief sought – receivership is not an independent remedy.

*Grand Lodge v. Shorter*, 122 So. 36 (Ala. 1929)

If the plaintiff does not seek a judgment against the defendant, there is no basis for the court to appoint a receiver.

*Stallworth v. Andalusia Hospital*, 470 So. 2d 1158 (Ala. 1985)

- The purpose is to prevent fraud or to preserve property during litigation.

*Irwin v. Irwin*, 148 So. 846 (Ala. 1933)

- Courts are cautious as this remedy usually interferes with established property rights.

*Ingram v. Omelet Shoppe, Inc.*, 388 So. 2d 190 (Ala. 1980)

- A plaintiff must properly plead that:

- The movant has a recognizable interest in the property.

*Allen v. Investors Syndicate*, 24 So. 2d 909 (Ala. 1946)

- Irreparable harm (i.e., loss or destruction) to the property will likely occur if this relief is not granted.

*Carter v. State ex rel. Bullock County*, 393 So. 2d 1368 (Ala. 1981)

However, immediate danger is not required in some situations.

*Underwriters v. Atlas Ins. Co.*, 108 So. 2d 687 (Ala 1958)

- No adequate legal remedy is available.

*C.E. Development Co. v. Kitchens*, 264 So.2d 510 (Ala.1972)

- The movant has a likelihood of success on the primary relief requested in the complaint.

*Ramage v. McDowell*, 151 So. 849 (Ala. 1933)

- Insolvency may be an important consideration to be pled by the movant.

*Martin Oil Co. v. Clokey*, 277 So. 2d 343 (Ala.1973)

However, insolvency alone will not justify a receivership.

*Davis v. Kemp*, 77 So. 745 (Ala. 1917)

b. Examples of Cases Where Receivership is Available

- Action for injunction to prevent removal of property in a business.

*Hunter v. Parkman*, 34 So.2d 221 (Ala. 1948)

- Action for ejectment from real property.

*Preuitt v. Wallace*, 189 So. 887 (1939)

- Action for judicial foreclosure (to intercept rents being wasted).  
*Albritton v. Lott-Blackshear Commission Co.*, 52 So. 653 (1910)
  - Action for a corporate accounting by minority shareholders.  
*Henry v. Ide*, 96 So.2d 698 (Ala. 1923)
  - Action to dissolve a partnership.  
Ala. Code § 6-6-723
  - Action to dissolve a corporation.  
Ala. Code § 10-2B-14
  - Action to set aside a fraudulent conveyance.  
*C.E. Development Co. v. Kitchens*, 264 So.2d 510 (Ala.1972)
- c. Examples of Cases Where Receivership is Not Available
- Unsecured creditors wanting to seize a defendant's property.  
*Cassells Mills v. First National Bank of Gadsden*, 65 So. 820 (Ala. 1914)
  - Refusal by an officer to let minority shareholders see corporate books.  
*Birmingham Disinfectant Co. v. Smith*, 56 So.721 (1911)
  - Business dispute not involving fraud or imminent loss of assets.  
*Hallman v. Brock*, 85 So. 280 (Ala. 1920)
- d. Other Considerations
- Only a circuit court has jurisdiction to appoint a receiver.  
ARCP Rule 66 (dc)  
*Woods v. Phillips*, 823 So. 2d 648 (Ala.2002)
  - Notice to all interested parties is required except in an emergency.  
*American Armed Services Underwriters, Inc. v. Atlas ins. Co.*, 108 So. 2d 687 (1958)
- Courts generally schedule a hearing because, except in extreme circumstances, lack of notice and a hearing may violate the Due Process Clause of the Fourteenth Amendment.  
*North Ga. Finishing, Inc. v. Di-Chem, Inc.*, 419 U.S. 601, 95 S.Ct. 719, 42 L.Ed. 751 (1975)

#### 4. The Requirement of a Bond

- A bond is required by statute, and it is usually supplied by the movant, not the appointed receiver.

Ala. Code § 6-6-622(a)

Ala. Code § 10-2B-14.32(b)

(Note that in a federal case, the receiver or a trustee in bankruptcy must supply his/her own bond.)

- Failure to require a bond is reversible error, but it can be waived.  
*Hunter v. Parkman*, 34 So.2d 221 (Ala. 1948)
- Persons damaged by wrongful appointment of a receiver may bring a separate action for damages up to the amount of the bond.  
Ala. Code § 6-6-622(b)
- No bond is necessary if the court has already entered judgment for plaintiff.  
*Tsimpides v. Hare*, 123 So. 2d 109 (Ala. 1960)

#### 5. Compensation

- There is no set schedule for a receiver's compensation as there is for a trustee in bankruptcy; a receiver's "reasonable" compensation is determined by the appointing court in its sound discretion.

*Carter v. Mitchell*, 142 So.2d 514 (Ala. 1932)

- A receiver's compensation and reimbursement of expenses is typically paid from the funds in the case as a first priority claim, even before payment of liens and owners' claims.

*Thornton v. Highland Ave. & Belt RR*, 10 So. 442 (Ala. 1892)

- The court can also divide the costs of the receivership among the parties.

*Carter v. Mitchell*, *supra*.

- There is specific statutory authority for the court to compensate the receiver's attorney in a corporate dissolution case.

Ala. Code § 10-2A-196

## **Part 2: Discussion of Receiver's Duties**

### **1. Initial Duties**

- a. Establishing a Bank Account
- b. Taking Control of Books and Records
- c. Beginning Periodic Reports to the Court
- d. Investigating the Company's or Individual's Financial History

### **2. Valuation of Property**

### **3. Demands for Turnover of Property**

### **4. Sale of Assets**

- a. Motion to Sell
- b. Sale Free and Clear of Liens
- c. Sale of Jointly-Owned Property
- d. Lump Sum versus Periodic Payments
- e. Auctions

### **5. Employment of Professionals**

- a. General Standards
- b. The Motion to Employ

- c. Supervising Professionals
- d. Fee Arrangements and The Motion to Compensate

**6. Executory Contracts and Unexpired Leases**

**7. Claims Bar Date**

- a. The Motion to Establish Filing Deadline
- b. Reviewing and Objecting to Claims
- c. Status of Tax Claims
- d. Status of Secured Claims

**8. Environmental Issues**

- a. Potential Federal (EPA) and State (ADEM) Liability
- b. “Chain of Title” Considerations

**9. Tax Considerations**

- a. Income Taxes
- b. Sales and Use Taxes
- c. Employment Taxes
- d. Property Taxes
- e. Filing Tax Returns

**10. The Final Report and Accounting**

- a. Accounting of Day-to-day Income and Expenses
- b. Request for Final Compensation
- c. Distribution of Remaining Funds
- d. Final Report to the Court