

E&O Issues for Commercial Property Receivers

The amount of properties in receivership has grown exponentially which creates both opportunities and challenges for the commercial real estate professional (CRP). With new opportunities for revenue, many CRP's are actively seeking receivership responsibilities in order to secure opportunities in management, leasing and eventual sales.

There are several E&O issues which can arise as a result of these new responsibilities:

Difference in the scope of their responsibilities

A Receiver's responsibilities are broader than that of a standard property manager. All orders require the Receiver to act as an independent party representing the creditors and court. The Receiver may have the responsibility to maintain the property, but also has the responsibility to collect debts, sue debtors, enter into leasing or even sell the property without court approval.

Many of these duties are not just transactional, they are also fiduciary. A real estate agent may not be aware of all the laws, regulations and duties of a fiduciary and their E&O policy may not extend coverage to these additional fiduciary services.

Receivership orders often are granted to an individual

Instead of to the corporation or companies This creates several issues:

1. Liability on a personal basis that cannot be protected by a corporate shell.
2. It may be argued that an individual court order is outside of the scope of work for the insured entity and therefore E&O policies may not extend coverage to the individual if the contract is only in the individual's name.
3. Receiverships most often require a bond which is an individual bond for the services. The applications for these bonds will require collateralization of personal assets. The application for will typically require personal financial statements, tax returns and provide a personal guarantee. If the receiver is married, typically the spouse will also have to sign the guarantee.

Indemnifications differ by jurisdiction

Receiver orders indemnify the Receiver for their duties in executing the court order and are afforded indemnification. However, every Receiver order is different –Many orders only limit the indemnification to "while acting within the scope of their duties except in cases of negligence."

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Contact our experts today to find out how you can protect your business.

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We believe this type of indemnification doesn't provide any protection for the Receiver. We are not lawyers and don't make any legal representations as Receivers should have their own legal counsel review all orders. However, it is our recommendation that you discuss with your counsel, gross negligence language and final adjudication language in all orders. In cases of adjudicated gross negligence, fraud or willful misconduct, your E&O policy most likely will not respond if the allegation is fraud.

Vacant Property Insurance Issues

If the underlying property is vacant or less than 31% occupied then the coverage offered is limited. Once a property becomes vacant, additional risks emerge - such as vandalism, theft, water damage due to pipe breakage and other similar risks. These types of risks emerge since no one is on the property on a daily basis and are not typically covered for vacant property.

A Receiver can ultimately be held responsible for making sure the property is properly insured and ensuring creditors and courts know the correct insured status of the underlying property. E&O claims can arise as a result of vacant property not being covered or being inadequately covered. Many CRP E&O policies specifically exclude failure to place insurance from their policies.

Conflicts of Interest

A court-appointed Receiver is typically appointed as an independent third party to represent the interests of the creditors and the courts. Commonly, a receiver is appointed to assess the current situation, maintain the underlying property and its value, oversee collection of debt, seek current revenue through leasing and eventually oversee the sale of the property. The receiver is often given the authority within certain financial parameters to carry out these services, enter into and execute contracts on behalf of the court.

CPM's often seek to become appointed so that their related real estate firms may make money on the services related to the receivership. Inherently this creates a conflict of interest. Although, it is a common practice to hire your own firm to provide these services, in all cases we recommend the court approve any contracts with related companies so that any conflicts are disclosed in advance and approved by the court. Many receiver orders authorize the receiver to sell the property and dispose of the assets. In many cases the sales price doesn't have to have court approval prior to sale.

We believe this is a significant risk to the Receiver. E&O claims can arise when creditors allege that the receiver should have obtained a higher sales price on the asset and thus the creditors suffered. We recommend any receiver contracts require approval of the court prior to any ultimate sale of the property or any long term leases. If the court order does not require it, then the Receiver should seek court approval prior to the sale.

These are just a few of the E&O issues we see relating to the services of a court-appointed Receiver. Please feel free to contact me to discuss any issues you may have regarding your contracts and how we might be able to assist you in properly insuring your services.

Contact our experts today to find out how you can protect your business.