

What Is a Receivership and How Does It Differ From Bankruptcy?

Creditor's Rights Toolkit

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This article will discuss the key differences between bankruptcy and receivership and what those differences mean from the perspective of a creditor.

A receivership is an equitable remedy in which an independent third party is appointed by a court to manage and preserve a business's assets. In most insolvency-related instances, a receiver is appointed to maximize the value of the secured lender's collateral. Though bankruptcy and receiverships are similar, there are significant important differences between the two insolvency proceedings.

Bankruptcy

Generally benefits the borrower who has become insolvent.

Governed and bound by the Bankruptcy Code.

Existing management maintains control of debtor in possession.

Discharge of debts.

Automatic stay and injunction of proceedings imposed by statute.

Lengthy and expensive.

Receivership

Benefits the creditor seeking to protect its security and creditors of the company.

Governed by applicable state or federal law and powers granted in order appointing the receiver.

The receiver is generally in charge of operations and decisions, though exact powers and duties will depend on appointment order.

No discharge granted.

Usually an injunction against litigation, but it depends on the specifics of the appointment order.

Can be swift.

KEY ISSUES

POWERS AND DUTIES

The receiver's powers and duties are derived mostly from the order appointing the receiver, but certain states have statutory schemes that govern a receiver's actions, powers, and duties. Generally, the receiver will be the ultimate decision-maker over the company's assets and operations during the receivership period. An appointment order will also likely contain authority for the receiver to market assets for sale and permit the sale upon further order of the court to generate distributions to creditors.

RECEIVER AS FIDUCIARY

Because a receivership is typically a remedy for secured creditors, unsecured creditors have a limited role in the proceedings. The receiver, as a fiduciary, has a duty to act in the best interests of the creditors and to manage or

preserve the receivership estate for their benefit.

STAY OF PROCEEDINGS

Unlike bankruptcy, there is no automatic stay of proceedings against the receivership assets that arises by operation of law. However, the appointment order will likely include an injunction against such proceedings. Creditors can move for modification of this injunction, just like seeking relief from the automatic stay.

MANAGEMENT OF RECEIVERSHIP ESTATE

The main purpose of a receivership is to conserve property value. Accordingly, the receiver must operate the property, and/or realize the value of the property with the diligence of an ordinary prudent person.

EFFECT ON CONTRACTS

A receiver does not have the power to reject or assume/assign executory contracts like a trustee or debtor in possession would pursuant to Section 365 of the Bankruptcy Code.¹ An appointment order could certainly give a receiver the power to terminate, enter into, or negotiate contracts, but this power is not accompanied by the statutory mandate that any defaults be cured prior to assumption.

DISTRIBUTIONS TO CREDITORS

A receiver will request that all creditors with a claim against the receivership estate file claims. After realizing proceeds from the estate (either through a sale of property or rehabilitated operations), the receiver will typically propose a distribution plan to the court for approval. Generally, the fees of the receiver and its counsel are paid first (and other administrative expenses), secured creditors are paid next, and general unsecured creditors after that.

TAKEAWAY

Overall, the receivership process can be a useful tool for secured creditors but does not allow for much involvement by general unsecured creditors. Creditors of a receivership estate should work with experienced bankruptcy counsel to monitor the proceeding and submit a timely proof of claim in order to properly protect their interests. Bankruptcy counsel can also maintain an open line of communication with the receiver or its counsel to stay up to date with the status of the proceedings.

Access this article and read other insights from our [Creditor's Rights Toolkit](#).

¹ See [What Is an Executory Contract and What Will Happen to My Executory Contract in Bankruptcy? tp_creditors-rights-toolkit_what-is-an-executory-contract.pdf](#)

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