

# North Carolina Commercial Receivership Act

**Presented by:**

- Charlie Livermon, Womble Bond Dickinson (US) LLP
- Michael L. Martinez, Grier Wright Martinez, PA
- Anna S. Gorman, Grier Wright Martinez, PA



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## Background and History of the Act

**History:**

- 2015-2018: Subcommittee of Legislative Committee of Bankruptcy Section Drafted Proposed Receivership Act
- Summer 2018: Section Council Approved Draft of Proposed Act
- Fall 2018: Proposed Act, with accompanying report (in materials), submitted to Board of Governors of NC Bar for inclusion in the Bar's 2019 Legislative Agenda and approved
- March 26, 2019: Proposed Act Filed in Senate as SB364
- May 2, 2019: SB364 (after several amendments) passes Senate 49-0 before crossover date
- June 25, 2020: SB364 (as modified) passes House 114-0 and Senate 49-0
- July 1, 2020: Signed by Governor as SL 2020-75 (copy in materials)
- January 1, 2021: Effective date of the new Act

**Background References:**

- Uniform Commercial Real Estate Receivership Act (adopted July 2016)(complete with prefatory notes and comments): <https://www.uniformlaws.org>
- Minnesota (adopted 2012); Minnesota Statutes, chapter 576
- Washington (adopted 2004); Chapter 7.60 RCW



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## Who Can Be a Debtor Under the Act

**NCGS 1-507.21(a) and (b):**

- Applies to proceeding where a receiver is appointed for an entity or an individual business debtor
- Individual business debtor is an individual whose consumer debts are less than 50% of his/her total debt on the date of filing of the receivership pleading (NCGS 1-507.20(b)(12b)
  - Caveat: Part 1 of Article 38 was not repealed by the Act so a receiver may still be appointed for an individual who is not an individual business debtor under NCGS 1-501, et seq.
- Exclusions to being a debtor under the Act:
  - Trust (other than a business trust)
  - Estate of deceased person, missing person, or absentee in military service



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## Differences in Limited and General Receivership

### NCGS 1-507.23– Two types of receiverships:

- Limited: Based upon foreclosure or enforcement of a security instrument– control over specific property
- General: Receiver is granted control over debtor and its operations
- Limited Receivership can be converted to General

### NCGS 1-507.28– Powers of Receivers:

- Subsection (a): General Powers of both – can manage partially exempt property pursuant to 1-507.45
- Subsection (b): Additional Powers of General Receiver – corporate authority & power to file bankruptcy
- Court can modify or expand powers and duties



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## Grounds for Appointment of Receiver

### NCGS 1-507.24 (c) – (g):

- Appointment of limited receiver (not general receiver) before judgment (a) to protect party that demonstrates right, title or interest in property that is subject of action; (b) if property or its income in danger of waste, loss or impairment; or (c) if property is about to be subject of voidable transaction (c is the only new ground for pre-judgment appointment).
- Appointment of limited or general receiver for any entity or individual business debtor after judgment (a) to carry judgment into effect; (b) dispose of property according to judgment; (c) preserve property pending appeal; or (d) execution returned unsatisfied and debtor refuses to apply property in satisfaction of judgment (all grounds same as existing statute – NCGS 1-502).
- Appointment of limited or general receiver for any entity or individual business debtor if debtor (a) insolvent, (b) not paying undisputed debts when due, (c) unable to pay debts as become due; (d) imminent danger of insolvency; (e) suspends business; (f) loses legal existence; or (g) the subject of a dissolution action (essentially same as NCGS 1-507.1; f and g new; but all of these grounds apply to individual business debtors).
- Appointment of limited receiver (not general receiver) in connection with foreclosure or enforcement of a security interest if (a) necessary to protect the property; (b) debtor agreed in writing to appointment upon default (loan documents/forbearance agreements, etc.); (c) the property and other collateral is not sufficient to satisfy the secured obligation; (d) debtor failed to turn over collateral to secured party; or (e) holder of subordinate lien obtains appointment of receiver (all new grounds).



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## Procedure for Appointment of Receiver

- **NCGS 1-507.24(a):** Appointment of a receiver may be the sole remedy sought in a civil action or it may be ancillary to other relief
  - Debtor can initiate its own civil action to appoint a receiver itself
  - Court now has jurisdiction to appoint a limited receiver in a power of sale foreclosure
- **NCGS 1-507.24(h):** Party seeking to appoint a receiver must give the debtor at least 10 days notice, but court may appoint a temporary receiver ex parte to avoid irreparable harm, subject to a later hearing
- **NCGS 1-507.25:** Eligibility of receiver – any person may serve as a receiver provided the person is qualified and is independent
  - Factors the court may consider in determining whether the proposed receiver is qualified and independent



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## Judge Assigned to Receivership

### NCGS 1-507.24(b) & 7A-45.4:

- Goal: consolidate proceedings under one judge until receivership ends
- Either a Superior Court or District Court Judge can appoint receiver for individual business debtor
- Only Superior Court Judge can appoint receiver for an entity
- Limited Receiver: Senior Resident Judge designates a Judge from the district or currently sitting in the district
- General Receiver for an Entity is appointed as 2.1 Judge
- Mandatory Complex Business Case: \$5 million in assets



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## Scope of Receivership Property

### NCGS 1-507.20(b)(24); 1-507.24(i):

- All receivership property is under control and supervision of court appointing receiver. NCGS 1-507.41(a)
- A receiver, either limited or general, has power to possess, collect, control, manage, conserve, and protect receivership property – similar in nature to bankruptcy concept of property of the bankruptcy estate
- Order appointing receiver must describe receivership property "with particularity appropriate to the circumstances". If order does not so describe the receivership property, default rule is that pending further order of the court receiver has control over all of debtor's nonexempt property
- In general receivership, receivership property is all or substantially all of the debtor's nonexempt property
- In limited receivership, receivership property is the debtor's nonexempt property that is described in the order appointing the receiver or a subsequent order
- Receivership property excludes only wholly exempt property – partially exempt property is receivership property
- Exceptions in general receivership of individual business debtor:
  - Principal residence if value is less than combined amount of all liens and rights of redemption and allowed claims of exemption
  - Any consumer good if value is less than combined amount of all liens and rights of redemption and allowed claims of exemption
- Court may limit general receiver's powers and authority to such part of receivership property that upon disposition will result in sufficient proceeds to pay creditors in full. NCGS 1-507.28(d)



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## Automatic Stay

### NCGS 1-507.42:

- General and Limited Receivership: prohibits any act, action or proceeding to obtain possession or control of receivership property or to enforce judgment against receivership property, except for an action to enforce a lien that is superior to the rights of the receiver in receivership property; or to create or perfect lien against receivership property NCGS 1-507.42(c)
- General Receivership: prohibits the commencement or continuation of any judicial, administrative or other proceeding against the debtor on any claim that arose before the appointment of the receiver or to enforce any lien having priority over the receiver in the receivership property NCGS 1-507.42(d)
  - Stay expires in 60 days unless extended by the court
- Court can modify the stay for cause upon request of a creditor NCGS 1-507.42(e)
- Stay inapplicable to exercise setoff, in criminal proceedings, to continue perfection of security interest NCGS 1-507.42(f)
- Sanctions allowed for violating the stay NCGS 1-507.42(h)



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## Notice of Administration of Case

### NCGS 1-507.34: Process for Notice to Creditors:

- (a) Notices of Appearance – any party may file. Not necessary to join parties. Proof of claim does not equal notice of appearance
- (b) Master Service List – Receiver must file within 30 days and update
- (c) Motions – follow Rules of Civil Procedure
- (d) Service – of motions and notices in accordance with Rule 5
- (f) & (g) Judge may enter orders without a hearing (when no objections are filed) and based on ex parte application (administrative matters)
- (h) Binding Effect



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## Suits by and Against the Receiver

### NCGS 1-507.38:

- Receiver may sue in the receiver's capacity
- Receiver may be sued in the receiver's capacity, but:
  - Receiver entitled to all defenses and immunities provided by law for an act or omission within the scope of his appointment
  - Receiver may not be sued personally for an act or omission in administering receivership property without approval of the judge presiding over the receivership proceeding
  - Party can conduct discovery of the receiver concerning any matter relating to his administration of the receivership property only after obtaining court order authorizing discovery. 1-507.27
- Venue of all suits by or against receiver or relating to the receivership or receivership property must be in the court where the receivership is pending, unless court orders otherwise
- For actions pending on the date of the receiver's appointment:
  - Receiver may be joined or substituted as a party if the action relates to receivership property
  - General receiver may be joined or substituted as a party if the debtor was a party to the action
  - May be transferred to the court in which the receivership is pending upon the receiver's or a party's motion made in the court in which the action is pending, provided that the transfer motion is filed no more than 90 days after the receiver's appointment



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## Exemptions by Individual Business Debtor

### NCGS 1-507.39:

- If exemptions have not been claimed, Receiver shall send notice of right to claim exemptions within 30 days after appointment
  - Debtor has 20 days to claim exemptions and receiver shall send the claimed exemptions to creditors within 10 days of receipt
  - Receiver and creditors have 10 days from service of exemptions to file objections
  - Receivership judge shall designate property as exempt and resolve valuation issues
- Exemptions designed before the appointment shall remain enforceable but may be modified upon motion by the receiver, a creditor who was not a party to the original designation, or the debtor
- In a limited receivership, this section only applies if the debtor has the right to claim an exemption in the receivership property



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## Sale of Receivership Property Free and Clear of Liens

### NCGS 1-507.46 – Use or Transfer of Property not in the Ordinary Course:

- Motion & Notice – 14-day period for secured creditor and debtor claiming exemption to object
- Sale Free & Clear – similar to Section 363 sale concept but broader
- Transfer of proceeds to liens in order of priority
- No sale can be approved if: 1) secured lien will not be paid in full and creditor objects and 2) the Court determines that the amount the creditor will receive is less than creditor would receive within a reasonable time in absence of the sale. Receiver has burden
- No sale of co-owner's interest in property
- Not required to be public auction
- Secured Creditor may credit bid (NCGS 1-507.46(e))
- Good faith protection for purchaser



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## Ability of Receiver to Borrow Money

### NCGS 1-507.44:

- Limited and general receiver can obtain unsecured credit or incur unsecured debt on behalf of the receivership without court approval
- On motion by the receiver and after notice and a hearing, limited and general receiver may obtain secured credit and incur debt secured by receivership property with prior court approval
- Any debt, unsecured or secured, is allowable as an administrative expense of the receivership. That administrative expense is paid after the payment of allowed secured claims, to the extent of proceeds from the disposition of collateral, but with the same priority as all other expenses incurred by the receiver during the receivership, including fees and expenses of the receiver and professionals employed by the receiver
- No provision for a priming lien absent consent of lienholder
- Presumably receivers may negotiate and include in the borrowing order a carve out with the lender providing the financing that would permit the receiver to receive approved compensation ahead of the lender



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## Compensation of Receiver

### NCGS 1-507.31: Compensation:

- Reasonable compensation without need for a court order
- Factors to be considered in determining compensation:
  - (1) agreement between the parties
  - (2) value of assets
  - (3) number and amount of claims
  - (4) time and labor expended
  - (5) novelty and complexity
  - (6) time and skill required
  - (7) receipts and disbursements
  - (8) distributions to creditors
  - (9) compensation in other receiverships

### NCGS 1-507.51(b): Surcharge of Collateral:

- If the proceeds to be distributed to the secured creditor are not sufficient to pay the lien and the receiver's fees and costs, the court may order the payment of those fees and costs from the proceeds to the extent the secured creditor received a direct and quantifiable benefit from the receiver's actions



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## Executory Contracts

### NCGS 1-507.20(b)(8) & 1-507.45:

- Similar definition to Bankruptcy Code – performance due
- Adoption, Performance, Assignment or Rejection – 90 days to adopt or reject or else rejected by operation of law
- Receiver can seek extension
- Ipso Facto concept – Receiver can still adopt contract
- Can assign with court permission according to state law
- Rejection = breach
- Claim for damages for rejection must be filed within 30 days or claims deadline



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## Executory Contracts

- Rejection of contract for the sale of real property where purchaser possesses property or holds timeshare interest – purchaser may terminate contract and claim lien on property for amounts paid OR retain possessory interest by performing
- Rejection of contract for unexpired lease of real property where debtor is landlord – Receiver may not reject: 1) where tenant's primary residence (certain conditions & exceptions); 2) Receiver appointed by other than secured creditor; or 3) lease is superior
- No specific provisions for Intellectual Property
- Claim for damages for rejection must be filed by the later of 30 days from the rejection or the claims deadline



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## Turnover of Receivership Property

### NCGS 1-507.40:

- Unless otherwise ordered by court, all persons in possession of receivership property must turn it over to the receiver and all persons owing a debt that is receivership property shall pay it to the receiver except to the extent that the debt is subject to setoff or recoupment
- Similar to §542 of Bankruptcy Code except that turnover is not automatic, it requires demand by the receiver
- If a creditor is in possession of receivership property and the validity of the creditor's lien depends on continued possession, the creditor may retain possession until it is provided with adequate protection of its lien
- Turnover is enforced by the receiver's filing a motion in the receivership
- If there is dispute over the receiver's or the debtor's interest in the receivership property, then the receiver must bring a lawsuit in the court where the receivership is pending. Similar concept as the bankruptcy requirement for filing an adversary proceeding to determine validity of liens or interest in property
- Absent a bona fide dispute, the court may sanction as civil contempt a person's failure to turn over receivership property to the receiver



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## Claims Process

### NCGS 1-507.49:

- The court will establish the claims process, including whether proofs of claim must be filed, the form of the proof of claim, where claims are to be filed and the deadline for filing.
  - Alternatively, the court may direct proofs of claim to be filed with the receiver
  - The court may allow claims based on the books and records without the need for filing proofs of claim

### NCGS 1-507.50:

- Receiver or any party in interest may object to a claim
- Claims for which no objection is filed or not disallowed by the court are deemed allowed
- Court may estimate contingent or unliquidated claims or the right of payment from an equitable remedy



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## Priority of Claims

### NCGS 1-507.51: Claims paid in order of priority on pro rata basis:

- Secured claims, in order of priority – Receiver may surcharge collateral
- Administrative claims accrued during the receivership
- Domestic support obligations – reference to 11 U.S.C. 101
- Wages – reference to 11 U.S.C. 507(a)(4) & (5)
- Consumer customer deposits tied to 11 U.S.C. 507(a)(7)
- Unsecured taxes
- Other unsecured claims
- Tenancy by Entireties doctrine respected



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Thank you!

**Q&A**



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