Servant of two masters? The receiver-manager's dilemma

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Introduction

In Nigeria, receivership tends to constitute the bulk of insolvency practice. It is also a preferred recovery technique for secured lenders because, ideally, it does not require the secured creditor to go to court to enforce security.\(^1\) An appointment that combines receivership with managership provides greater flexibility, and the terms of the appointing instrument confer powers on the receiver-manager that go beyond those traditionally acknowledged by statute.

However, inasmuch as a privately appointed receiver-manager is expected to work for the principal, there are also fiduciary obligations to the debtor company under statute.\(^2\) In practice, this may result in a conflict of interest. Consequently, the receiver-manager must walk a fine line in order to avert personal liability and post-receivership litigation from the debtor company. This update sheds light on this tension and suggests a few ways in which to maintain the balance.

Role and powers

Role

Section 567(3) of the Companies and Allied Matters Act, as amended, defines a 'receiver' to include a manager. In practice, secured lenders (ie, banks and other financial institutions) tend to ascribe the same role, obligations and powers to receivers and receiver-managers, although the Nigerian courts have clearly held otherwise. For instance, in *Ponson Enterprises (Nig) Ltd v Njigha*\(^4\) the Court of Appeal held that:

> "The fact that the word 'receiver' is interpreted in section 650 of the Companies and Allied Matters Act as including 'a manager'... does not invest a receiver with the powers of a manager. The interpretation does not change the legal character, connotation or comprehension of the two concepts."

In consonance with the classic distinction given by Sir George Jessel MR in *Re Manchester and Milford Rly Co*,\(^5\) the Supreme Court also clearly distinguished between a receiver and a manager in *Uwakwe v Odogwu*,\(^6\) stating that:

> "A receiver as such has no authority to carry on a going concern. His duty is to stop the business, collect the debts and realize the assets... A manager, on the other hand, has powers to continue a business or any going concern."

Section 393(1) of the act states that:

> "A person appointed [as] a receiver of any property of a company shall, subject to the rights of prior incumbrancers, take possession of and protect the property, receive the rents and profits and discharge all out-goings in respect thereof and realise the security for the benefit of those on whose behalf he is appointed, but unless appointed manager, he shall not have power to carry on any business or undertaking."

Powers

It has been stated that:

> "the powers of a privately appointed receiver and manager depend upon the terms of the debenture under which he is appointed, subject always to any statutory provisions affecting those powers... Many of the powers are express
Where a person is given express authority to pursue a cause of action, he or she has implied authority to do whatever is necessary for, or incidental to, the effective execution of his or her express authority in the usual way.

It appears to follow that, subject only to the supervision or sanction of the court in the case of a receiver or manager appointed by the court, extra-curial and curial receiver-managers are vested with broad powers with which to discharge their duties. The powers, which are akin to those given to directors during the normal life of a company as a going concern, are listed non-exhaustively under Section 393(3) and Schedule 11 of the act and may be categorised generally as:

- the traditional powers of a court-appointed receiver to take possession of, deal with and dispose of the assets and properties of the company;
- the traditional powers of a director to:
  - raise capital or borrow funds on the basis of the company's assets as underlying collateral;
  - authorise and prosecute or defend legal actions in the name of, and on behalf of, the company (including powers to rank and claim in the bankruptcy, insolvency, sequestration or liquidation of any person indebted to the company and to receive dividends, and to accede to trust deeds for the creditors of any such person); and
  - use the company seal;
- carry on the business of the company in the most beneficial manner possible;
- enter into beneficial contracts;
- invest or call up any uncalled capital of the company;
- employ or dismiss employees; and
- obtain and maintain insurance in respect of the company's business and property;
- the power to make arrangements or compromises on behalf of the company or to present or defend a petition for the winding-up of the company; and
- the power to appoint an agent to conduct business that he or she is unable to conduct or that can more conveniently be conducted by an agent.

The provisions of Section 393 make clear that where a receiver-manager is privately appointed over all (or substantially all) of the company's assets, all powers listed in that section and in Schedule 11 are deemed to be included in his or her powers, as expressly stated under the debenture instrument whereby he or she was appointed. Where these statutory default powers expressly conflict with powers contained in a debenture instrument, the provisions of the debenture shall prevail.

**Extra-curial receiver-managers: duties and dilemma**

In practice, an appointment by the court on the application of an interested person is usually for the appointee to act as receiver of a company property or asset. However, even where such an appointment involves the receiver acting as a manager, there appears to be little difficulty, as such a receiver or manager is deemed an officer of the court, acting in accordance with the court's directions and instructions. As a fiduciary of the court, he or she is meant to preserve or realise the property, assets or funds entrusted to him or her. He or she is also largely insulated from the interference of any parties in dispute.

The situation of privately appointed receiver-managers is different. Their duties and obligations can be seen as deriving both from the appointing instrument and from statute. In this case, the receiver-manager first owes a duty to the relevant regulatory authorities to comply with statutory requirements to give notification of appointment and discharge and periodic reports on his or her stewardship (including the filing of a statement of affairs).

However, under the instrument of appointment, the receiver-manager is clearly mandated to act as an agent on behalf of his or her appointors to protect their interests (ie, to ensure the realisation of security and optimal recovery of the debt). This goal is consistent with the personal interest of a privately appointed receiver-manager, as the remuneration of such an insolvency practitioner is usually negotiated on the basis of a percentage of recoveries.

Like directors and other managers of a company as a going concern, the insolvency practitioner is in a fiduciary position in relation to the company and is bound to act in utmost good faith. Moreover, he or she may be held personally liable for contracts into which he or she enters, unless such a contract expressly specifies otherwise.

As such, practitioners cannot simply dance to the tune of their principal appointors and...
ignore their fiduciary obligations as defined in statute. Rather, in practice they attempt to balance the interests of their appointors and other stakeholders, including the best interests of the company itself.

Most of the provisions of the act justify this shift in focus from the exclusive interest of the creditors to the best interests of the company generally and other stakeholders. This can also be seen as a shift from a strict liquidation approach to a business rescue approach, which aims to leave the company to run as a going concern once the practitioner has discharged the role of realising the appointor's security. The relevant provisions of Sections 390 and 393 are as follows.

Section 390 provides that:

"(1) A receiver or manager of any property or undertaking of a company appointed out of court under a power contained in any instrument shall, subject to section 393 of this Act, be deemed to be an agent of the person or persons on whose behalf he is appointed and, if appointed manager of the whole or any part of the undertaking of a company he shall be deemed to stand in a fiduciary relationship to the company and observe the utmost good faith towards it in any transaction with it or on its behalf.

(2) Such a manager shall:

(a) act at all times in what he believes to be the best interests of the company as a whole so as to preserve its assets, further its business, and promote the purposes for which it was formed, and in such manner as a faithful, diligent, careful and ordinarily skilful manager would act in the circumstances;

(b) in considering whether a particular transaction or course of action is in the best interest of the company as a whole may have regard to the interests of the employees, as well as the members of the company, and, when appointed by, or as a representative of, a special class of members or creditors may give special, but not exclusive, consideration to the interests of that class.

(3) Nothing contained in the articles of a company, or in any contract, or in any resolution of a company shall relieve any manager from the duty to act in accordance with subsection (2) of this section or relieve him from any liability incurred as a result of any breach of such duty."

Section 393(2) provides that:

"A person appointed manager of the whole or any part of the undertaking of a company shall manage the same with a view to the beneficial realization of the security of those on whose behalf he is appointed."

Sections 390(2) and (3), which seek to establish mandatory fiduciary obligations for a receiver-manager, are made subject to Section 393, which clearly acknowledges that the receiver-manager's loyalty is to his or her appointor, and that the priority is to realise the underlying collateral to the loan transaction. Nigerian jurisprudence on the meaning and construction of the phrase 'subject to' in a statutory provision is quite settled: it postulates that a provision which is made subject to another provision or statute shall be subordinated, governed, controlled and restricted in its meaning and application by the governing provision or statute. To that extent, it may be argued that a receiver-manager can never be faulted for always giving priority to the interests of the principal.

However, if this were so, there would be no practical need to appoint a manager in addition to a receiver. Moreover, although Section 390(1) acknowledges the relationship between receiver-manager and appointor, Sections 390(2) and (3) stress the need for the receiver to act in utmost good faith towards the company and to take account of the interests of employees, shareholders and other classes of creditor in the discharge of his or her actions. Furthermore, it voids any contractual stipulation or resolution of the company, ousting the need for a receiver-manager to comply with such fiduciary obligation and exempting him or her from liability for failure to adhere to this statutory duty. It is settled law that a statute must be complied with when it prescribes the doing of a thing.

The essential rationale of appointing receivers as managers is to enable them use their managerial and professional skills - with or without the help of other professionals appointed by them - to return a failing company to profitability if possible, acting in that company's best interests. Best practice also envisages that as a matter of priority, such insolvency practitioners should:

- assess the company and the viability of the business; and
- propose solutions that are geared to returning it to profitability, which includes its ability to meet its commercial obligations to its creditors.
The tremendous risk of abuse and fraud which accompanies the conferring of such broad powers over a company's assets justifies the imposition of such fiduciary obligations and other professional obligations. Regrettably, experience has shown that in the absence of statutory regulation of the insolvency profession, some practitioners have indulged in unprofessional practices, with little in the way of disciplinary penalties. Companies to which a receiver-manager has been appointed out of court sometimes remain in receivership for several years without returns being made by the receivers, making it impossible to determine whether debts have been liquidated or security realised. There are insider dealings and sales to interested third parties; assets are sometimes sold at an unjustifiable undervalue. In such cases, the receiver and possibly the principal have captured and hijacked the company to enrich themselves or their associates unjustly. They do this by using the broad powers available to insolvency professionals, to the detriment of other stakeholders (including employees and other unsecured creditors). By the time an interested creditor can apply for winding-up, there may be no assets to realise and distribute without prejudice to the powers of a liquidator to void certain contracts or scrutinise potentially fraudulent transactions carried out before winding-up.

Comment

There is a clear need for greater regulation and professionalism in insolvency practice.

Privately appointed receiver-managers should act in the most professional manner possible. A receiver-manager who uses the option under Section 391 to apply to the court for direction in relation to a matter arising in connection with the performance of his or her duties or functions may succeed in adroitly averting interference on the part of the appointor, since the court has latitude and discretion to make such orders as it deems fit.

As a professional, a receiver-manager who takes control of a debtor company's business and assets must first assess the options available. The receiver-manager may choose to manage and carry on the business of the company if he or she finds that the company's problem is improper management or a temporary and remediable cash flow issue. Where the business is still viable, the receiver-manager may choose to insulate it from the problems of the debtor company by transferring the viable portion of the business to a subsidiary special purpose vehicle that is floated for that purpose, particularly for existing (but not yet completed) contracts with change of control clauses.

In any case, the receiver-manager should provide sufficient materials to its appointor and the court to allow for a determination of the best approach, and should give directions that serve the best interests of the company and avoid unnecessary litigation against the receiver by directors of the debtor company. It is unacceptable for a receiver-manager to remain in control over a long period without a definitive strategy to realise the assets of the company or implement a business recovery plan.

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Endnotes

(1) Usually, securities such as mortgages or debentures include the right to appoint a receiver to realise or enforce the security, including by means of private sale. However, in practice the first instinct of a debtor company’s directors is normally to seek injunctive reliefs from the court with the aim of frustrating the exercise of the power of sale.

(2) Companies and Allied Matters Act 2004, CAP C20 LFN 2004.

(3) Formerly Section 650 of the act.

(4) [2000] 15 NWLR (Pt 689) page 46, at 48.

(5) (1880) 14 Ch D 645, at 653. It was stated that: "a receiver is a term which was well known in the Court of Chancery as meaning a person who receives rents or other income paying ascertained outgoings, but who does not, if I may say so, manage the property in the sense of buying and selling or anything of that kind... if a receiver was appointed... the trade stopped immediately. If it was desired to continue the trade at all it was necessary to appoint a manager, or a receiver/manager... He could buy and sell and carry on the trade."

(6) (1899) 5 NWLR (Pt 123) 562.


(9) These powers can validly be expanded further, beyond the provisions of statute, in the contract between the lender and the borrower, although no such clause may
operate to oust the core obligations and duties of the receiver. Similarly, Section 279(8) of the act prohibits the ousting of a director’s core duties through the company’s articles or resolutions.

(10) In circumstances where there is a dispute before the court and the assets are also in jeopardy, the court will appoint an “indifferent person between the parties to a cause... to receive and preserve the property or fund in litigation, and receive its rents, issues, and profits, and apply or dispose of them at the direction of the court when it does not seem reasonable that either party should hold them.” (See Black’s Law Dictionary, sixth edition, page 1268.)

(11) Section 389(2) of the act.

(12) Picarda, ibid, page 127: “The duties of a receiver manager appointed under a debenture consists of duties imposed by statute, duties imposed expressly upon him by his appointment and duties that arise out of his peculiar status... while being primarily answerable to the debenture holders who appointed him.”

(13) Namely, the Corporate Affairs Commission. However, the act does not expressly envisage proper monitoring and supervisory powers on the part of the commission; nor does it give the commission powers to take measures against an errant receiver for non-compliance or bad stewardship (unlike the position where the receivership is based on court appointment).

(14) Sections 396 to 399.

(15) See Sections 279 to 283, and particularly Sections 279 and 280 on fiduciary obligations and directors’ conflict of duties, compared with Section 390(2).

(16) Sections 390(1) and (2).

(17) Section 394(1).


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